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Politics this week

Jan 15th 2004
From The Economist print edition

A demanding ayatollah

Reuters

The American-led administration in **Iraq** was in a bind after the country's most influential Shia Muslim cleric, Ayatollah Ali Sistani, again insisted on direct elections to an interim parliament that is supposed, under the Americans' current plan, to choose a full-fledged Iraqi government by July. The Americans still want the parliament to be chosen by caucuses of notables. Tens of thousands of protesters took to the streets of Basra demanding direct elections.

See article: Iraq's leading ayatollah tries to call the shots

Though the **United Nations** says it has no plan to send back staff who were withdrawn from Iraq after the UN's headquarters in Baghdad were blown up in August, a UN team will visit the city in the next fortnight to look at security and transport arrangements in case the organisation does decide to return.

Deputies staged a sit-in in parliament after **Iran's** highest body, the conservative Guardian Council, where the country's ayatollahs hold sway, disqualified about half the 8,200 people hoping to stand in next month's parliamentary election. Those banned included 80 incumbent MPs.

See article: The state of Iran

Friends of Ariel Sharon, **Israel's** prime minister, continued to fend off charges of improper election-campaign funding after a tape of a business transaction involving him—but so far deemed legal by the official election-monitoring body—was aired on Israeli television.

See article: Israel and the Palestinians

A Palestinian suicide bomber killed herself and four Israelis at a Gaza crossing-point to Israel. In a break with usual practice, the Palestinian prime minister, Ahmed Qurei, declined to condemn the attack.

See article: Palestinian hardliners gain ground

Poor **Swaziland's** King Mswati ordered nine new palaces to be built to house seven current and two future wives at a cost of £8m ($14.5m).

The road to Iowa

The Democratic presidential contenders held their last debate before the **Iowa caucuses**. A new poll showed that Howard Dean and Wesley Clark (who is skipping the Iowa event) are the clear favourites among Democratic voters nationwide.

See article: The struggle in Iowa

Paul O'Neill, George Bush's first treasury secretary, alleged that the administration began preparations to invade Iraq soon after taking office in January 2001. He also claimed that Mr Bush was like “a blind man in a room full of deaf people” when it came to decision making. The Treasury has asked for an investigation into Mr O'Neill's possible misuse of classified documents.

See article: Paul O'Neill tells his story

The Supreme Court said it would not hear a case on secrecy procedures used by the Justice Department when it detained and then deported over 700 foreigners, mostly Arabs and Muslims, in the aftermath of the **September 11th attacks**. An appeals court has already agreed with the administration that releasing the names of the individuals could compromise intelligence-gathering operations.

See article: Guantánamo Bay

Mr Bush unveiled ambitious plans to build a **lunar base** and then to put a man on Mars.

See article: Pie in the sky

Arnold Schwarzenegger unveiled his first budget as **California's** governor. The $99 billion plan proposes cuts in spending on education, health and welfare programmes, but no tax increases. He said that if his bond proposal did not succeed in a ballot in March, the state would face a $14 billion deficit.

At the summit

Heads of state from north, south and central America met at a “special” **Summit of the Americas** in Monterrey, Mexico. There were arguments over trade, among other things. George Bush's new immigration scheme met with some approval, but a dispute between Brazil and the Unites States over immigration checks continued. In retaliation for American measures partly designed to detect terrorists, Americans entering Brazil are being photographed and fingerprinted.

See article: Hot air at the Summit of the Americas

In a surprising reversal of policy, Mr Bush announced that Canadian companies would be eligible to bid for future reconstruction **contracts in Iraq**. France and other critics of the Iraq war are still shut out of the bidding.

Demonstrations designed to oust President Jean-Bertrand Aristide of **Haiti** continued. Mr Aristide says he is willing to hold fresh elections.

AFP

See article: Continuing unrest in Haiti

Happy new year?

Sri Lanka's president, Chandrika Kumaratunga, caused a row when she claimed she was entitled to an extra year in office. She was inaugurated for her second six-year term, in 1999, a year earlier than she needed to be, she says.

The prime minister of **India**, Atal Behari Vajpayee, said he hoped elections would be called in April, six months early. A train from Pakistan crossed into India for the first time in two years, marking a further thaw in relations between the two countries.

See article: India's reinvigorated prime minister

South Korea's foreign minister “resigned” for not reflecting official policy. Not critical enough of America, said the rumours.

Losing immunity

Italy's constitutional court dealt another blow to **Silvio Berlusconi**. It ruled that a law passed last June giving the Italian prime minister and four other top officials immunity from prosecution was unconstitutional. A trial of Mr Berlusconi on judge-bribing charges, which was suspended last July, is now likely to resume.

See article: Silvio Berlusconi

The European Commission is to take European governments to the European Court of Justice for breaking the **stability and growth pact**, which sets ceilings on euro-area countries' budget deficits. Last November, the governments overruled a commission recommendation that France and Germany should trim their deficits this year, and sought to put the pact in abeyance.

See article: The stability pact and the European Court

After pressure from Turkey, a coalition government was formed in **northern Cyprus** that will seek to reopen unification talks with the Greek-Cypriot south. Turkey is anxious to begin negotiations on accession to the European Union: but the EU has made clear that, if Cyprus is still divided when it joins in May, the Turks will have little chance.

See article: A shift on northern Cyprus

Germany's armed forces are to be shaken up. The army will be cut in size and made more professional, but the defence minister, Peter Struck, said that conscription will remain. There was no hint of more defence spending: Germany spends less on defence as a proportion of GDP than other big NATO countries.

See article: Germany reforms its armed forces

Getty Images

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Business this week

Jan 15th 2004
From The Economist print edition

Consolidation

The wave of consolidation in America's financial industry continues. **J.P. Morgan Chase** announced plans to take over Chicago-based **Bank One** for $58 billion in shares. This will cement its position as America's second-largest bank after Citigroup.

See article: Another big merger

A French court ruled that **Morgan Stanley** had issued investment research that was biased against LVMH causing it "financial and reputational harm" while puffing the performance of **Gucci**, a rival luxury-goods firm and a client of the American investment bank. Morgan Stanley was ordered to pay LVMH *euro*30m ($38m) to compensate for damaged "morale" while a further payment for material damages is assessed.

See article: A blow to independent research

Meanwhile, **Sodexho** asked French regulators to investigate **Smith Barney**, Citigroup's investment-banking arm. The bank issued an analyst's report revealing what it claims was debt unacknowledged in the catering firm's accounts. Sodexho said that the arrangement had been disclosed in the accounts of a subsidiary.

Leo Kirch filed lawsuits in America that accuse Deutsche Bank and Liberty Media, a cable-TV firm, of conspiring to bring about the collapse of his media empire in 2002 in order to "carve up the spoils".

Looking for a bargain

Enron's former finance chief, Andrew Fastow, and his wife, Lea, struck a plea bargain with prosecutors that will see Mr Fastow get a ten-year sentence. His co-operation could help prosecutors to bring criminal charges against Kenneth Lay and Jeffrey Skilling, former bosses of the fallen energy trader.

See article: Trying times

Adecco's shares plunged by over a third after the temporary-employment agency admitted to "material weaknesses in internal controls" at its North American businesses and delayed publication of its accounts for 2003. The shares recovered slightly after Adecco assured investors that it did not face a Parmalat-style accounting scandal, but the precise nature of the problem remains unclear.

Creditors of **Bank of Credit and Commerce International** went to court to pursue a claim for damages of £850m ($1.6 billion) against the Bank of England. They claim that the Bank acted in bad faith by refusing to investigate or to close BCCI, which collapsed in 1991 with debts of some £7 billion. The Bank of England denies the charges.

Under-insured

Iain Lumsden quit as chief executive of **Standard Life**. Britain's biggest mutual insurer had fallen foul of new methods for calculating its capital base introduced in the wake of the near demise of Equitable Life in 2000. The insurer announced that it would raise £750m ($1.4m) of new capital and that it was ready to abandon mutual status in favour of a stockmarket flotation.

Creditors of **LG Card** agreed to a 5.3 trillion won ($4.5 billion) bail-out to save South Korea's biggest credit-card company from bankruptcy. State-run Korea Development Bank stepped in to ensure that the deal succeeded by agreeing to cover any losses not covered by the bail-out and will manage LG Card until it is sold in a year or so.

Mutual distrust

The reputation of **America's mutual-fund industry** suffered another blow. The Securities and Exchange Commission is considering action against several brokerages for steering customers to mutual funds in return for payments. The SEC believes the practice to be widespread, and proposed new rules forcing the disclosure of fees, expenses and any conflicts of interest to investors.

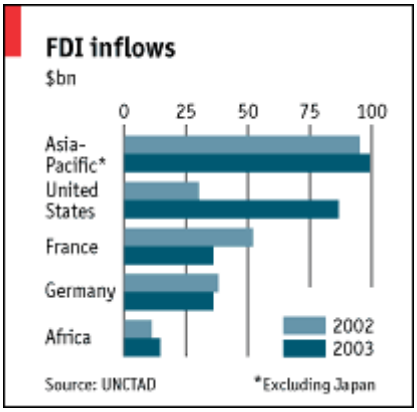
See article: The SEC acts

America's **E*TRADE** said that it was in talks with Toronto-Dominion Bank that could reportedly lead to a merger with the Canadian bank's **TD Waterhouse** unit to create the world's second-largest discount brokerage.

Nasdaq announced a pilot scheme that will see shares of six companies, including Hewlett-Packard and Charles Schwab, that are listed on the New York Stock Exchange traded on its market too. Since 2000, 119 companies have moved from Nasdaq to the NYSE but only one has made the reverse journey. Nasdaq may hope that the recent travails of the NYSE could persuade more companies to loosen their links with its bitter rival.

Borders of finance

Foreign direct investment, an indicator of the progress of globalisation, remained flat at $653 billion in 2003, down from a peak of $1.4 trillion in 2000, according to UNCTAD. Economic uncertainty led to a decline in cross-border mergers though foreign investment in America tripled as its economy recovered strongly. UNCTAD predicts that FDI will rebound in 2004 as the world economy improves.



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Manned spaceflight

A grand but costly vision

Jan 15th 2004
From The Economist print edition

Publicly financed space-exploration should be about science not political grandstanding

AP

Get article background

IN THE past week, plans for a manned lunar base, and a subsequent trip to Mars, were leaking from Washington, DC, almost as fast as air from the international space station. Was President George Bush testing the water to see if his bold vision would be a vote winner? If that was the plan, he would not have liked the response even before he announced it formally in a grand speech on January 14th (see article). Despite public delight at the success of the current robotic Mars missions, one of the earliest polls (by AP/Ipsos) on the idea of returning humans to the moon and then advancing to Mars suggested that most Americans think the money would be better spent domestically. As one of those polled so eloquently put it, “You can't have a war, cut taxes, have the economy in a garbage pail and spend billions going into space.”

The proposals actually turned out to be more modest than the rumours, though they do focus the efforts of NASA, America's space agency, even more heavily on human spaceflight than at present. They involve an “extended human presence” on the moon, in order to use it as a stepping stone for human missions to Mars and to worlds beyond. But even modest proposals in space can be costly. So although the big spending on these ideas is actually scheduled for the never-never-land beyond the possible incumbency of Mr Bush, it is still fair to question now whether they would be wise things to do.

On the face of things, it does not appear so. Adding it up, human spaceflight has cost America more than just the lives of astronauts. The Apollo moon programme cost approximately $100 billion in 2002 dollars. The shuttle has cost about $150 billion since its birth in 1971, according to research from the University of Colorado. And the still-unfinished space station has cost $25 billion so far.

Nor does anybody really know how much Mr Bush's proposals will end up costing, and the bitter lesson of the past is that it is unwise to believe the figure that is given at the outset. Tripling any such number would be a start. Realistically, a 10-15-year return-to-the-moon programme, if run by NASA in the usual way, would cost tens of billions of dollars. For this cash, Americans will get to watch a handful of people roam not very far on the lunar surface, and they will have the huge satisfaction of knowing they have returned before the Chinese make their first visit. As to the price of Mars and beyond, the sky is, as it were, the limit.

Bottling moonbeams

Thinking optimistically, it is just possible that all this flimflam is actually a cunning plan to scuttle the shuttle once and for all. NASA has resolutely clung on to this old, dangerous and costly vehicle. Part of Mr Bush's project involves ending the shuttle programme in 2010. Offering the agency the moon tomorrow—complete with all the flashy new hardware required to get people and materials up there—in exchange for a shuttle-retirement plan today would be a clever ploy. Plans for running around the moon could then be scaled back by future budget cuts. From the sound of it, though, Mr Bush means what he says, and his plans look like the latest in a long line of “bold visions” proposed to transform NASA.

Ironically, it was an obsession with the moon which got NASA into its current mess. The original moon race was, of course, far more about ideology than science. Money was lavished on the moon-shot primarily to prove which system—communist and restricted, or capitalist and free—would prevail. NASA's victory seemed to answer that question.

The riches of Apollo, however, are NASA's albatross today. The agency was built, and remains constructed, in a mindset of central planning in which it exists largely to spend lavish billions from government on uncommercial and unjustifiable projects. But bold government visions and expensive white elephants such as the shuttle and manned flights to the moon do little to advance human knowledge.

Even many space enthusiasts now warn that only private enterprise will truly drive human expansion into space, and yet America's government keeps ignoring them. What might cause market forces to take up the mission? Tourism and entertainment are both possibilities. It may seem surprising, but there are large numbers of people who would spend hundreds of thousands of dollars on a trip into space. Two people, so far, have spent $20m, and another two are on their way. Film and television companies would also spend tens of millions if they could. One might laugh at the television concept “Stars in space”, but people would watch it. More to the point, though, is that no one's government would be paying for it.

My favourite Martian

But what makes NASA's human-spaceflight programme most unfortunate is that it consumes two-thirds of the agency's budget, and squeezes the scientifically useful things (such as the Mars rovers) that the agency does, and does well. That is likely to get worse with the budget reallocation that Mr Bush is proposing in order to pay for his plans. Last year, the House of Representatives' Committee on Science was warned that “the net impact of people on a spacecraft is to greatly limit its range and capabilities, without adding any value that can begin to compensate.” The best estimate is that putting people on a spacecraft multiplies the cost ten-fold. But nobody has taken any notice.

The true space entrepreneurs in America, the people who are building realistic, privately funded spacecraft for tourism, and moon satellites for entertainment, have had no government hand-outs or incentives. They push on regardless. They are the pioneers most worth applauding.

As for the fault in all this sorry mess, it lies as much with the blindness of the politicians that have directed NASA over the years as it does with the agency's reluctance to let anything, or anyone, else share its monopoly on space. Ideas and visions are two a penny. Finding the best way to advance knowledge of the vast complexities of outer space—to boldly go where no man has gone before intellectually rather than just physically—is the real challenge.

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Sub-Saharan Africa

Making Africa smile

Jan 15th 2004
From The Economist print edition

Bad leadership has crippled Africa. But there are, at last, signs of recovery

Panos

"BLASPHEMOUS" was how the information minister described an article in the *Zimbabwe Independent* complaining about President Robert Mugabe's habit of commandeering commercial passenger jets for his own use. It was a revealing choice of adjective. Mr Mugabe's henchmen do not really think their leader divine, but they often suggest that he is infallibly righteous, and that those who defy him should be smitten. The *Independent*'s blaspheming scribes were perhaps lucky to be released on bail this week.

Zimbabwe provides a dramatic illustration of how statist economic policies, corruptly enforced, swiftly impoverish. In the past five years, Mr Mugabe's contempt for property rights has made half the population dependent on food aid, while his cronies help themselves to other people's land and savings, and build helipads for their own mansions. But Zimbabwe's curse is also Africa's. The main reason the continent is so poor today is that Mugabe-style incompetent tyranny has been common since independence (see our survey). The most important question for Africans now is whether Mr Mugabe represents not only their past, but their future as well. There are encouraging signs that he does not.

Consider first the advance of democracy south of the Sahara since the end of the cold war. In the 1960s and 1970s, no African ruler was voted out of office. In the 1980s, one was. Since then, 18 have been, and counting. That still leaves a lot of countries where polls are rigged and dissidents disappear, but it is surely a sign that some African governments are becoming more accountable to their people.

Africa's media, too, are shaking off their shackles. Under most of the military regimes of the 1970s and 1980s, independent newspapers and radio stations were simply not allowed. Today, they are as numerous as they are irreverent. Television is still largely state-controlled and journalists are still persecuted—occasionally in most countries, systematically in places such as Zimbabwe and Eritrea—but, overall, the mighty are subject to greater scrutiny than before, which makes it a bit harder for them to abuse their power.

In the past couple of years, Africa has also grown more peaceful. During the cold war, the great powers fought a series of proxy battles on African soil, arming and aiding each other's clients' enemies with scant regard for the African lives their meddling cost. With the collapse of the Soviet Union, Africa's strategic importance waned. Its wars, however, did not. Without their superpower backers, some states crumpled, leading to new and exceptionally bloody struggles in countries such as Congo and Liberia.

Fortunately, several of these conflicts seem at last to have run their course. Angola and Sierra Leone are at peace. The pointless border clash between Ethiopia and Eritrea has stopped. Congo's war, the worst anywhere since the second world war, is formally over. Liberia's warlord, Charles Taylor, has been driven into exile. Even in Sudan, which has known only 11 years of calm since 1962, government and rebels are on the verge of signing a power-sharing deal.

This sudden outbreak of tranquillity has various causes. Angola's war stopped because one side won. Others have ended because both sides were exhausted, or because outsiders cajoled them into putting down their weapons and starting to talk. If Sudan's rulers make peace this year, it will be largely because they are terrified of what George Bush might do to them if they do not.

A long trek ahead

It is too early to say that Africa has turned a corner, however. Sporadic but brutal fighting continues in Burundi, Côte d'Ivoire, eastern Congo and western Sudan, among other places. There is still a risk that new wars may begin, or old ones reignite, for many of the causes of Africa's instability have yet to be resolved.

Because political office is a quick route to wealth in Africa, people fight for it. Since most Africans feel more loyal to their tribe than to the young and artificial nation-states of which they are nominally citizens, it is often easy for unscrupulous leaders to win support by appealing to bigotry. Because Africa is poor and economically stagnant, there are a lot of jobless young Africans for whom joining a rebel group and looting the village next door can seem like an attractive career option. AIDS makes Africa even poorer, and so less stable, although some recent studies suggest that it may affect slightly fewer millions than previously estimated (see article).

If Africans are to have a chance of pulling themselves out of penury, they need governments that do not stand in their way. They need leaders who uphold the law impartially, but otherwise let people do what they wish. They need governments that pass sensible budgets and stick to them. Fiscal realism is more common now than a decade ago, as the continent's generally lower inflation rates attest. But graft is still widespread: Angola's rulers were accused this week of having wasted or misappropriated $4 billion in five years—more than 9% of GDP each year. (They denied it, of course.)

Africa's two most important countries—Nigeria and South Africa—are doing several things right. Both have swapped tyranny for democracy, and both are using their diplomatic and military muscle to end some of their neighbours' wars. But both governments are worryingly dependent on a single source of revenue: oil, in Nigeria's case, and white taxpayers, in South Africa's. If Africa as a whole is to prosper, the majority of its citizens will have to produce more, fashioning goods or providing services that the rest of the world wants to buy. Given that most Africans are subsistence farmers, that will not be possible without a vast social upheaval, with unpredictable consequences. It is a daunting challenge, but the alternative is likely to be worse.

Rich countries can help Africa, ideally by removing the tariffs and farm subsidies that throttle African trade. But in the end it is up to Africans to solve their own problems, starting with the ejection of some of their current rulers. The Big Men will not go quietly; but they are not immortal, either.

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Emerging economies

What's in a name?

Jan 15th 2004
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It is hard to tell when an emerging economy has emerged

FOOTBALL fans care passionately about whether their home team is in the first, second or third division. Countries feel the same about their economic ranking. Ten years ago this month, *The Economist* launched its emerging-market indicators page, and still by far the most popular question asked by readers is how we decide whether an economy should be listed as “developed” or “emerging”.

It would be nice to give a simple answer. Economies used to be categorised by whether or not they were a member of the Organisation for Economic Co-operation and Development (OECD), the so-called “rich-man's club”. This was always a bit crude: Turkey, a long-standing member, is relatively poor. But now the OECD is a real mixed bag, and includes such newcomers as Mexico and Poland. Nor can we at *The Economist* claim to rank economies rationally by income per head: Hong Kong and Singapore (still listed by us as emerging economies) both have a higher income per head than Italy. Taiwan and South Korea have also now, more or less, caught up with Portugal and Greece, which (in the full set of tables on our website) we count as developed economies. Our sorting is largely driven by convenience: it seems awkward to split Hong Kong and Singapore from China and Malaysia.

The truth is that traditional economic labels are less and less useful. “Industrial economies”, the old name used for rich countries, is now meaningless: industry accounts for only 16% of jobs in America, for example—much less than that in poorer countries. The old “third world” label has been replaced by “developing” or “emerging” economies to portray a more positive image. But the breakdown of the old categories has bred confusion. Different organisations and banks use different groupings. For instance, the United Nations and J.P. Morgan Chase count Hong Kong, Singapore, South Korea and Taiwan as developing (or emerging) economies. Morgan Stanley Capital International's emerging-market index includes South Korea and Taiwan, but Hong Kong and Singapore are in its developed-markets index. The International Monetary Fund counts all four as “advanced economies”.

Some years ago, frustrated by the old labels, we proposed a three-way split: paralysed economies (mainly poor ones in Africa); progressing economies (notably China and India, which are growing rapidly); and the paranoid (rich economies, such as America, which fear competition from the progressives). For some reason that escapes us, this scheme did not catch on. So further ideas on how to re-label economies would be welcomed, by e-mail to suggestions@economist.com.

How should we solve our immediate problem of deciding when an economy has progressed from emerging to advanced status? Our economics team could perhaps vote each year on which economies

deserved promotion or relegation. An alternative, more in tune with *The Economist's* philosophy, could be to let the market decide. There is excess demand for a limited number of slots on our developed economies page, so these slots could be auctioned to the highest bidder. But a word of warning: promotion to a higher league is not always cause for celebration. Mexico joined the OECD in 1994, just before the “tequila” financial crisis. The IMF promoted South Korea, Hong Kong, Singapore and Taiwan to advanced-economy status in May 1997, only months before East Asia's financial collapse. Moving into *The Economist*'s first division might turn out to be a leading indicator of economic trouble.

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Mexico and the United States

A chance for both sides of the border

Jan 15th 2004
From The Economist print edition

A boost for George Bush, and maybe for Mexico's president too

EPA

IT WAS like old times again. Like most such jamborees, this week's special Summit of the Americas in Monterrey failed to sort out very much (see article). But it did see a rapprochement between the host, President Vicente Fox of Mexico, and his most important guest, President George Bush of the United States. It was not just that their quarrels about the Iraq war were put aside. Both men seemed to have recovered part of the reputations they enjoyed when they won election in 2000—Mr Fox as a modernising internationalist, Mr Bush as a compassionate conservative.

The credit for this turnaround should go to the bold plan Mr Bush launched just before the summit to "legalise" the 8m-12m illegal immigrants living in the United States. Mr Bush wants these people, around half of whom come from Mexico, to become temporary guest workers; after three years they would have to renew their permits.

There are all sorts of reasons to be cynical about Mr Bush's scheme: it is a blatant attempt to win Latino votes in an election year, its chances of getting through Congress are slim and more details need to be given. But it is plainly a big step in the right direction. The system of "don't ask, don't tell" has ensured a lot of cheap gardeners and building workers; but it cannot be in America's interest to have so many of its occupants beyond the law. Mr Bush's solution would keep immigrants coming to America, but make their passage safer.

Mr Bush's willingness to be "pro-immigrant" (as governor of Texas, he could hardly have been anything else) was one of the points that marked him out in 2000. Might Mr Fox, who came to power as an energetic reformer, also recover some of his own *élan*? Despite his expertise at glad-handing at international conferences, the words commonly associated with his government have been inertia, drift and impasse. Until this week, the immigration issue with America was a prime example of his inability to change things. Just possibly, he may be able to use the more positive mood to start to unlock the rest of his reforming agenda.

Not all Mr Fox's problems are of his own making. Despite his victory in the presidential race, his National Action Party failed to gain a majority in the congressional elections and did even worse in last summer's elections at mid-term. This has allowed Mexico's old ruling dinosaur, the Institutional Revolutionary Party (PRI), to obstruct almost all his reforms. Among the blocked measures are urgent proposals to ease Mexico's sclerotic labour laws and allow private investment in the energy sector. Fiscal reform is even

more urgent. Mexico's government takes a paltry 12% of GDP in taxes. This is low even by regional standards, and catastrophic by world standards. Without more revenue, this now middle-income country cannot begin to address the problems that all Mexico's politicians acknowledge, such as rotten schools and crumbling infrastructure.

Nonetheless, his own poor strategy has compounded Mr Fox's problems. He raised expectations so high on coming into office that Mexicans were bound to be disappointed when the results were mediocre. His government has also proved to be inept at forming the sort of congressional alliances that are needed to get things done in Mexico's newly pluralistic system of politics. He has come to look like a peripheral president, incapable of taking action while Mexico is overtaken by China, the Caribbean and Central America in the race for foreign investment and jobs.

The immigration lifeline from Mr Bush is not likely on its own to transform Mr Fox's fortunes. But it will surely help. And Mr Fox has recently been given another glint of light with the opening up of a rift within the PRI. The opposition party is now divided on reform, with about one-third of its members in Congress claiming to favour what the president is trying to do. Though the odds are against him, Mexican politics is still in flux and the reform debate might yet be won—if Mr Fox can find a way to seize the moment.

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Iran

Two governments, both duds

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From The Economist print edition

Most Iranians seem to want regime change. They may have to wait for it

AP

IF A house divided cannot stand, Iran has long been due for collapse. Its two parallel governments, one theocratic, one democratic, have been on the worst of terms for several years. Now some at least of the democrats seem in a mood for a showdown. Provoked by the disqualification of about half the 8,200 people hoping to stand in next month's parliamentary election, several prominent democrats are said to be ready to resign (see article). Were they to do so, the long power struggle between democratic reformists and conservative clerics might take a decisive turn, leading perhaps to the definitive end of the theocracy ushered in by the 1979 revolution.

All the signs are that such an end is deeply desired by most Iranians. The clerics who wield nearly all the formal power in Iran have failed on almost every score. Their fierce adherence to religious dogma, with its bans on alcohol, satellite television and most social mixing of the sexes, has become a huge irritation. Their foreign and security policies have brought Iran isolation and condemnation, first for promoting terrorism abroad, more recently for seeking to acquire illicit nuclear weapons. And their economic failures are even more distressing. Though Iran sits on 10% of the world's known oil reserves and more gas than any country but Russia, GDP per person was about 30% higher in the days of the shah. Central planning, suspicion of foreign investors and general mismanagement have resulted in a dearth of jobs—a matter of special concern to the two-thirds of the population under the age of 30.

This is the country the supreme religious leader, Ayatollah Ali Khamenei, likes to call a model for all others. He takes pride, no doubt, in the constitution's democratic features. Yet Iran's vaunted democracy is becoming ever more obviously a sham. Newspapers are closed with tedious regularity. Journalists, students and political activists are routinely arrested. Demonstrations are broken up and dissenters silenced.

Disillusionment all round

It was in protest at such treatment that Iranians first elected a reformer, Muhammad Khatami, as their president in 1997. Though virtually all his efforts at liberalisation were thwarted by the clerics, he was re-elected in 2001. Fellow-reformers swept to victory in other polls, but they, too, suffered similar rebuffs at the hands of the mullahs. Eventually, some 18 months ago, Mr Khatami pronounced himself fed up and demanded the passage of two bills, one to rein in the judges who had done so much to nullify his

reforms, the other to curb the Council of Guardians, the body that vets election candidates and new laws. If the bills were not passed, said Mr Khatami, he would resign. Some threat: neither bill has become law, nor has Mr Khatami achieved any other significant reform. Yet he remains in office. Indeed, for all the reformists' brave vows, their promised showdowns have all come to naught.

The voters feel doubly let down, first by the corrupt and repressive clerics, now by the spineless democrats. When they last had the chance to vote, for city councils in February 2003, most chose to stay at home. Turnouts of 10-15% in the large cities handed victory to the conservatives, who could probably have won next month's poll in the same manner. The Council of Guardians, however, was not ready to risk failure.

The mass ban could have turned out to be a ham-fisted mistake, had the reformists been more popular: students might have mounted protests, as they have before, inspiring others to join in. Instead, this episode looks like ending either in compromise—as Mr Khatami publicly hopes, and Mr Khamenei seems to hint—or in a climbdown by the democrats. Only if the result is violent crackdown might the regime have any real cause for concern, for one day an ill-judged show of force could prompt an upheaval that throws the hated mullahs out.

What can outsiders offer to hasten that day? Not much, beyond moral support. One mistake they must avoid is to allow the regime's opponents to be plausibly cast as agents of the West. The shah was fatally contaminated by the American-British coup that brought him to power in 1953—a western-promoted regime change whose consequences still rack the world today. This time Iran's fate should be left to Iranians.

But will they ever act? At present, the regime's opponents are leaderless, unorganised and apparently powerless. Yet the clerics' power would not necessarily, or indefinitely, prove overwhelming in the face of people power. In recent years seemingly invincible governments have been peacefully ejected in, among other places, Georgia, Serbia, Chile and the Philippines. Sooner or later, Iran's turn will come.

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European corporate governance

The pause after Parmalat

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Europe's Enron calls for a measured, but more determined response

WHEN Enron imploded in 2001, America responded quickly and vigorously to a huge fraud. Politicians used the Enron affair as a wake-up call for American businesses. Tough new rules were introduced, notably the Sarbanes-Oxley act. Managers were told to sharpen up their standards. One of the world's biggest accounting firms disappeared, its reputation shattered by the actions of a few employees. Briefly, the integrity of the entire capitalist system seemed under threat.

The collapse into bankruptcy of Parmalat, an Italian dairy-products group, has become Europe's Enron. Billions of euros are missing. A once-respected firm is in tatters. Thousands of jobs are at risk. This European scandal shares many elements with the American one, from corrupt management and a complacent board of directors to complicated financial dealings in offshore tax havens via big banks, which seem to have been only too willing to underwrite the deals that kept a massive fraud alive for years. As at Enron, at the heart of the fraud lay an accounting and auditing fiasco (see article).

Yet how has Europe responded? So far, with little of America's vigour. In fact, the response has been rather muted. Plenty of observers want to dismiss the affair as a local Italian matter. After all, didn't Silvio Berlusconi's government water down penalties for false accounting? And isn't Italy a model of disregard for rules on corporate governance, a place where the rights of minority shareholders are regularly abused?

Unfortunately, these truths conceal as much as they reveal. As more has emerged about the fraud at Parmalat, it has become clear that the proper context for analysing it is a European one. There is an important Italian dimension, to be sure. By quickly changing its bankruptcy law and proposing a sweeping reform of its regulatory system, Italy has shown that, despite doubts, it may yet be capable of overcoming its normal political torpor. The decision this week by Italy's Constitutional Court to overturn a law which granted Mr Berlusconi legal immunity while in office also shows that the country's judiciary is not supine (see article). And yet while Mr Berlusconi runs the government, any reforms that touch the corporate sector will be tainted by the suspicion that they are designed for his benefit, or at least to do his interests no harm.

The real lessons for Europe are broader. The fraud at Parmalat gulled not only Italians but international investors, banks and credit-rating agencies. Parmalat even had an American listing for some of its securities to add to its air of normalcy. In short, the fraud has exposed how vulnerable the financial system remains when safeguards are perverted, either deliberately or through incompetence. The main

aim should be to make frauds easier to detect and harder to perpetrate. Strengthening auditing standards and compliance, as well as the role of truly independent board directors, is essential.

The European Commission has already suggested that it would like to strengthen auditing standards, perhaps by insisting that member countries introduce accounting-oversight boards, like the one required in America by Sarbanes-Oxley, to enforce the implementation of international accounting rules that will become obligatory for all EU companies next year. That seems sensible. In addition, the commission should try to impose more onerous standards on Europe's many securities exchanges. Tougher requirements on firms that want to list shares or sell bonds create a strong incentive for businesses to be open about what they are doing and make it much easier for outsiders to make informed judgments. In the short term, pressure can be exerted locally, by encouraging national exchanges (including Italy's) to adopt stricter rules. Longer term, as markets and exchanges consolidate, such rules should converge on a European-wide benchmark.

Rainbow regulation

Even such modest initiatives as these, however, are difficult. Parmalat is a reminder that Europe still has a long way to go towards the harmonising of either accounting or corporate-governance standards on best practice. Businesses operate amid a patchwork of rules and securities markets, and fraudulent firms can exploit this. Harmonisation need not mean a straitjacket of uniformity. Long-standing cultural differences will justify some variation. Nevertheless, it is in Europe's long-term interests to reduce the sheer intricacy of the current patchwork, especially because EU enlargement will inevitably add some vibrant new colours.

Doing so will require determination and political co-operation. National governments should support any efforts made by the commission to generate better practices and standards, starting with the basic building blocks of corporate auditing and accounting. If that is Europe's response to Parmalat, then Europe's businesses will all be better for it.

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Letters

Jan 15th 2004
From The Economist print edition

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Greater Europe

SIR – Attitudes towards Europe are indeed almost religious in their fervour ("The history of an idea", January 3rd). You cite the Roman empire, Charlemagne, Napoleon and even Hitler as valuable historical lessons but you skip several hundred years of European unity provided by the Roman Catholic church. What about Innocent III and other popes, and the college of cardinals? What about the government and legal system that the Catholic church gave Europe in the period between the end of the Roman empire in the west and the Congress of Vienna?

Vince Budrovich
Torrance, California

SIR – You stop short of connecting the Roman empire with the European Union of tomorrow. Your map of Rome in 117 shows clearly that it was wrapped around the Mediterranean, which the Romans proudly called *Mare Nostrum*. Greater Europe, to coin a phrase, embraces Turkey, Lebanon, Israel, Egypt and much of the Maghreb. Too much Europe even for you?

Ranko Bon
Motovun, Croatia

Mary, quite the contrary

SIR – You usefully remind us of the common links between Judaism, Christianity and Islam ("A Mary for all", December 20th). However, the example of Mary is not helpful in practice. The three religions do not agree among themselves, let alone with each other, about the role of women. Abraham (Ibrahim) is a much better common link. Through Ishmael, his first son, Abraham is the father of the Arab nations; through Isaac, his second son, he is the father of the Jews; and he is father by adoption to Christians for, according to the Bible, Abraham was the father of all who are acceptable to God because of their faith.

Alan Griffith
London

SIR – It is quite obvious that Judaism was a primary source of inspiration for the Koran, and that both Jesus and Mary are highly revered in it. To do justice to the Koran you should have quoted relevant verses from it, for example:

> Behold! the angels said: O Mary, God hath chosen thee and purified thee, above the women of all nations.
>
> Sura Al-Imran, verse 42.
>
> And remember her who guarded her chastity: We breathed into her of our spirit, and we made her and her son a sign for all peoples.
>
> Sura Anbiyaa, verse 91.

Ahmet Ozgunes

Istanbul

SIR – As an atheist, I have difficulty in considering the three religions as of more than historical interest. Nevertheless, a Madonna and child, whether an exquisite painting or statue in a museum, or a mother and child in the local supermarket, is surely one of the holiest of images. It should be no surprise that Mary is near the centre of these religions.

Mike Fuller
Honolulu

SIR – You say that "it can be hard for 21st-century observers to understand the sheer passion of the language that was addressed to Christ's mother in late antiquity." Rest assured, the masses have never forgotten:

> When I find myself in times of trouble
> Mother Mary comes to me
> Speaking words of wisdom
> Let it be.

David Glantz
Fairfax, Virginia

The rating game

SIR – Your article about Parmalat suggests that the company "failed to disclose lots of information" to Standard & Poor's, yet we maintained its rating at investment grade ("Déjà vu all over again?", December 20th). This is not the case. Parmalat and its advisers repeatedly provided us with detailed information about its liquidity position and its liabilities, in response to our inquiries throughout the year and as recently as December 5th. This essentially confirmed the audited accounts. That information was enough to warrant our lowest investment-grade rating (BBB-), but has now been shown—just like the audited accounts themselves—to have been utterly misleading.

Rating agencies are not auditors or investigators and are not empowered or able to unearth fraud. They depend on truthful audited public accounts and honest private information from the entities that they rate. It is easy to be wise after the event, but before Parmalat missed its bond repayment on December 8th—and was immediately downgraded by S&P—there was no indication that it faced an imminent liquidity crisis. On the basis of the public and private information available to us about Parmalat, we have acted in a responsible and timely manner.

François Veverka
Executive managing director
Standard & Poor's
Paris

Kill a whale?

SIR – Your article on whaling is correct in stating that lack of demand, by itself, will prove to be an important brake against over-exploitation, when and if more whale stocks are subject to controlled harvesting ("A bloody war", January 3rd). Yet you fail to discuss perhaps the most important argument in favour of whaling: the ecosystem approach to management. In the North Atlantic, the harvesting of all marine mammals has been at very low levels for more than three decades, a consequence of irresponsible behaviour by a number of environmental groups. This has caused substantial increases in the populations of whales and seals at the expense of fish stocks such as cod and haddock. In this context, harvesting of the more abundant marine mammals takes on a real economic significance.

Trond Bjorndal
London

SIR – You point to the disingenuous arguments of many of those who campaign for the abolition of commercial whaling but you fail to convey the cynicism of the whaling industry. Having insisted for years that they were capable of managing a sustainable industry, the pro-whalers have shifted emphasis to claim that whaling is essential because whales are consuming so many marine resources. Apart from the

shockingly poor science underpinning this argument, the notion of “culling” whales to protect fish stocks directly contradicts the idea of conducting a sustainable hunt that allows populations to grow.

Furthermore, as you note, there is no overwhelming demand for whale meat and products; there is barely any market at all. The industry is pushed and supported to benefit the political agendas of a select few. Under such circumstances it is legitimate to ask not why the whaling industry should be prevented from plying its trade but why it should be permitted to do so.

Kieran Mulvaney
Las Vegas

Leaden prose

SIR – Your obituary of Robert Bartley says that what he believed “flew out of his word processor like shards of white-hot lead” (January 3rd). Mr Bartley, who deemed materialism too important to be left to Marxists, would never countenance such vaporising. Lead liquefies without incandescence and evaporates at white heat.

Russell Seitz
Nantucket, Massachusetts

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Iran

Their last chance?

Jan 15th 2004 | TEHRAN
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AFP

While reformists protest, the conservatives are relentlessly gaining ground

Get article background

IN THE view of Mohsen Mirdamadi, one of Iran's most senior politicians, it smacked of a *coup d'état*. On January 11th the Council of Guardians, the iron fist of Iran's formidable clerical establishment, let it be known that it was barring some 4,000 candidates, including 82 serving deputies, from standing in parliamentary elections due on February 20th.

Officially, most of the disqualified candidates are being penalised for their supposed indifference to Islam and to the constitution, and for querying the virtually limitless powers enjoyed by the supreme leader, Ayatollah Ali Khamenei. No one doubts that they have been chosen because they support the country's reform-minded president, Muhammad Khatami, and his dangerously democratic ideas.

The Council of Guardians may be hoping to dissuade Iranians from voting. Last year's council elections, when the reformists lost power in most big cities, showed that a low turnout favours the conservatives. They hope that their stable 15%-or-so of the vote will win them a disproportionate share of parliament's 290 seats.

Ever since their sweeping victory in the last parliamentary election, in 2000, reform-minded deputies have backed the president in his struggle against Iran's roundly disliked, but immensely powerful, conservative institutions. Denied much of their legislative clout, parliamentarians have been reduced to using the chamber to highlight—but not, alas, to curb—the conservatives' abuses of power.

The Council of Guardians duly avenged itself on the biggest party of whistle-blowers, the Participation Front; just two of its 67 serving deputies were cleared to stand. In Tehran 52% of all candidates were barred. In distant Kurdistan, where ethnic nationalism wears reformist colours, the figure was 59%.

Since rumours of mass disqualifications had circulated long before they were made public, the barred parliamentarians had prepared their response. On January 11th about 80 deputies began a sit-in in the parliament building, to go on “as long as necessary”. If the council refuses to back down, says Reza Khatami, one of parliament's two deputy speakers (and the president's younger brother), the agitation

will grow and will “take new forms”.

To the regime's external enemies, these words are a portent—of political implosion, perhaps, foretelling the fatal weakening of the Islamic Republic. In Iran, a different view prevails. Rarely, since President Khatami's triumphant election in 1997, has the establishment seemed so powerful, or its eventual victory so assured.

The Guardians' grip

For the past four years, parliament has been undermined by hardliners. *Kayhan*, the conservatives' favourite newspaper, has taken pot shots at the “economic criminals”, “foreign lackeys” and “violators of public morals” who occupy it. Occasionally, conservative thugs have beaten up deputies. Most damaging of all, the Council of Guardians has sapped parliament's credibility as a chamber for making laws.

On the face of it, parliament's four-year report card is starred with enlightened legislation. Since 2000, deputies have, *inter alia*, liberalised a tough press law and made Iran subscribe to United Nations conventions outlawing torture and sex discrimination. They have legislated to expand trial by jury, devolve powers to local councils and ban the police from entering universities. But the Council of Guardians has spiked every one. Last October, when a reformist newspaper totted up parliament's record, it found that the council had vetoed 111 out of a total of 295 bills that parliament had ratified.

The shooting down of a particular set of bills, tabled by President Khatami, set the stage for the current confrontation. One had laid down strict criteria for the barring of candidates from running for public office; the other had enshrined the president's right to reverse the sort of flagrant violations of the constitution that conservative institutions have indulged in.

Reuters

Khatami, stymied

President Khatami and his supporters have not always reacted intelligently to these provocations. Reza Youssefian, one of the protesting deputies, acknowledges that the reformists have lost credibility by hinting repeatedly that they would withdraw from public life in protest at conservative obstructionism, and never doing so.

In 2001 the president threatened not to stand for re-election. He ended up standing, and won by a landslide. Later, through his aides, he let it be known that he would certainly resign if his two bills were shot down by the Council of Guardians. The bills were spiked, but the president did not budge. On January 13th, he threatened to resign again over the sit-in and take the protesting deputies with him: “We will all leave together,” he said. But he remains.

Perhaps partly because of this, only the government, the foreign media and the slender reformist press have paid the sit-in much attention. Millions of Iranians are still unaware of it. For the majority who do not read newspapers, the sole source of news is the hardline state broadcasting monopoly, Sound and Vision, which has so far refused to mention it. Even those Iranians who read reformist newspapers, or listen to the BBC, seem unmoved. In 1999 students at Tehran University responded to the banning of a reformist newspaper by mounting a spectacular protest that lasted several days. The class of 2004, by contrast, seems keener on swotting for exams. A proposed student sit-in was squashed by the university authorities.

Nor, concedes one of three barred female deputies, have Iranian women taken much note of events. Why should they, when the reformists have done so little for them? Over the past four years, most of parliament's limited attempts to redress gaping legal imbalances between men and women have been stymied by the Council of Guardians. Besides, President Khatami has appointed no women as ministers.

The president has responded to the current crisis with a mixture of coyness and caution. He condemned the disqualifications but asked the deputies to suspend their sit-in while secret talks continue. For some, it is hard to reconcile today's Mr Khatami, the backroom dealmaker, with yesterday's inspirational statesman who promised to institute openness and the rule of law. The deputies' defiance cannot disguise the fact that the president's reform movement has run out of steam.

This does not mean that the movement was worthless, or has achieved nothing. No one who remembers

Iran before Mr Khatami was elected would dispute that it has changed. Since 1997, Tehran has become a more humane, even permissive, place. Seven years ago, anyone taking a drive with a member of the opposite sex, or wearing make-up, was punished by jail or a lashing. These activities are still crimes, but the authorities now turn a blind eye.

On Mr Khatami's watch, Iran's human-rights record has become a bit less appalling. He himself is tolerant of criticism. Despite the banning of dozens of reformist publications, some good newspapers cling on. And dissidents are no longer summarily killed by hit squads; they are tried, albeit with scant regard for justice, and then locked up.

Iran is more open to foreigners than it was before Mr Khatami came to power. The government's swift acceptance of foreign aid after last month's earthquake in Bam stood in contrast to the rejection of similar offers that followed Iran's last big quake, in 1990. The Council of Guardians has even been persuaded to ratify legislation designed to attract foreign investment.

Despite the shadow cast by the tensions between Iran and America, foreign relations have proved President Khatami's greatest success. Besides making friends with countries, like Saudi Arabia, that sided with Saddam Hussein during the Iran-Iraq war of the 1980s, he charmed the European Union into starting talks on a trade pact and oversaw improved ties with countries, like Turkey, which Iran used to vilify for dealing with Israel.

An impossible contradiction

Yet Mr Khatami was elected only on a promise to reform his country as much as its theocratic structure would allow. And at the heart of Iran's strange semi-democracy lies an impossible contradiction. Although Iranian leaders like to claim that the Islamic Republic's legitimacy derives from its famously lively elections, everyone knows that the real influence lies in the hands of men, mostly clerics, who never have to face the voters.

Many Iranians had hoped that Mr Khatami could persuade the most senior of these, the supreme leader, to relinquish some of the powers that he enjoys under Iran's oddly incoherent constitution. That has not happened. Mr Khamenei is not impressed by the two massive endorsements that the president has received from the electorate. He senses a threat from uppity reformist deputies who, only last summer, elliptically called on him to step aside. He remains defiantly answerable to God and an assembly of clerics whose members he has a strong hand in selecting.

EPA

Khamenei, in charge

Mr Khamenei has likened himself to a referee at a keenly contested football match. On January 14th, cajoled by Mr Khatemi, he ordered the Council of Guardians to confirm the eligibility of all the sitting-in deputies who had not committed crimes. But he was presumably aware of the council's plans, since every member is either his appointee or the appointee of his appointee. According to Mohsen Kadivar, a reformist, the supreme leader shows his red cards only to one team.

The scope of the recent disqualifications is a sign of reviving self-confidence among the conservatives. For the past two years, their authoritarian instincts have been checked by the immense international pressure and scrutiny to which Iran has been subjected. That pressure started at the beginning of 2002, when George Bush included Iran in an “axis of evil”. The United States had already invaded one of Iran's neighbours, Afghanistan, and was turning its attention to another, Iraq. Many Iranians were convinced they were next.

That impression grew last year, as Iran squirmed in the spotlight shone by the International Atomic Energy Agency (IAEA). Evidence presented by the agency suggested that Iran had broken its treaty obligations and was alarmingly close to acquiring the technology needed to build a nuclear bomb. Last autumn the IAEA's board of governors demanded that Iran put its programme in cold storage.

Conservative sermonisers duly fulminated against the IAEA and America; hardline military commanders refused to allow agency inspectors into their bases. This, in effect, sabotaged the reformists' efforts to accommodate the agency's demands. Then, on October 21st, came a surprising U-turn. Iran undertook to reveal the sources of its nuclear technology, suspend its uranium-enrichment efforts and open

suspected nuclear sites to spot inspections.

The Rohani effect

One immediate result of this capitulation was to lighten the international pressure on Iran. It may also turn out to have determined the domestic balance of power. The decision to agree to the agency's demands was taken by Mr Khamenei, but the supreme leader did not depute the president to negotiate the details. Instead, he chose Hassan Rohani.

Mr Rohani holds no elected office. He is the supreme leader's representative on a bipartisan body called the Supreme National Security Council (SNSC). During his talks with the Europeans he made it clear that he carried Mr Khamenei's full authority, an impression the president could never have conveyed. The foreign ministers, tired of empty reformist promises, were seduced.

Iran seems to be abiding by its nuclear promises. The message is clear; the conservatives can be trusted. Mr Rohani's elevation suggests, too, that the conservatives are gathering the reins of foreign policy. Next year, when Mr Khatami steps down, the conservatives anticipate that one of their own will replace him. Not unreasonably: the Council of Guardians is expected to prevent all reformists from standing.

Mr Rohani now looks like a foreign minister in waiting. Since last October's deal, he has been respectfully received in Brussels and Moscow. His globetrotting at Mr Khamenei's behest has the effect of making the government look irrelevant.

AP

Appeals that go unheard

A conservative imprimatur is being more clearly felt on other Iranian policies. The most important of these is Iraq. The United States no longer suggests that Iran is out to destabilise its western neighbour. Iran is a good friend to four influential members of the American-appointed Governing Council. It sends petrol, officially and unofficially, across the border. The Revolutionary Guard gets on with coalition forces that control the areas contiguous to Iran. Iran's softer Iraq policy may stem from fear of American intentions; it certainly depends on conservative will.

So, too, do tiny hints of change in Iran's attitude to Israel. State radio may still devote hours to the murderous misdeeds of the “Zionist entity”, but conservatives no longer have their old appetite for confrontation. Mr Khamenei is unlikely to concede, publicly, Israel's right to exist, or to give up his paternal interest in Hizbullah, the Lebanese militia which Iran started in the 1980s. But the proposed restoration of full relations with Egypt, the first Arab state to make formal peace with Israel, is a telling instance of Iran's new pragmatism.

From their lair in the parliament building, the reformists view all this with wry amusement. The reform movement, they remind visitors, has sincerely sought to reconcile Iran with the world, only to be thwarted by conservatives. It was the conservatives, they recall, who stymied Mr Khatami's overtures to Bill Clinton. Now the same conservatives are interested in striking a deal with the Americans.

The aid that the United States sent to the victims of last month's earthquake in Bam may have been, as the administration said, humanitarian in purpose. The offer to dispatch a high-level mission to the afflicted region was more overtly political. Many Iranians rather like the Americans; but because the

regime officially does not, the offer was deferred. But there may be other chances to repair the relations that were severed with the takeover of the American embassy in Tehran in 1979. The Americans are less worried about Iran's nuclear ambitions than they were, and would like to encourage more Iranian co-operation in Iraq.

One hardline voice?

Iran's western interlocutors, whether American or European, will face the same dilemma. The slow rise of conservatives in the supposedly democratic parts of government means that, increasingly, foreign governments must work with the least enlightened parts of the Iranian system.

As Iran's nuclear capitulation showed, there are advantages for the West in this. Powerful conservatives, like Mr Rohani, can deliver more than well-intentioned but ineffective reformists. Yet Mr Rohani may prove an awkward friend. Europeans and Americans insist that Iran become more responsive to its people, and the conservatives are reluctant democrats.

That much was underscored by the mass disqualifications. In the conservative view, barring reformists is part of an effort to unite the two branches of Iranian decision-making, elected and unelected. By next summer, when Mr Khatami is replaced, they want Iran to speak with one voice. At present, they are being thwarted by 80 truculent parliamentarians.

Whatever the outcome, Mr Khatami and parliament, supported by a few newspapers, are all that prevent conservative institutions from taking an even stronger grip on the country. This is why the sit-in in Tehran, viewed with indifference by most Iranians, is so important.

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The Iowa caucuses

The hour of battle is at hand

Jan 15th 2004 | DES MOINES
From The Economist print edition

AP

Howard Dean is under pressure in Iowa, particularly from Dick Gephardt, but he is still the only candidate with a national machine

A MONTH ago it looked as if it was all over even before the fat lady entered the room. Howard Dean had swept the board in all the pre-primary primaries. He had won the fund-raising primary by raising an unprecedented amount of money—more than $5m a month in the second half of 2003. He had won the innovation primary by making superb use of the internet. And he had won the organisational primary by turning a crowd of angry Democrats into a disciplined army of “Deaniacs”. Buzz, momentum, enthusiasm: the former governor of Vermont had it all.

Now the fat lady is about to sing and suddenly things are much more confused. On January 19th Iowans vote in the caucuses that traditionally kick off the American primary season, and Mr Dean finds himself under pressure from Dick Gephardt, with John Kerry and John Edwards closing in. Some 10% of potential caucus-goers claim that they have not made up their minds and another 40% say that they are open to shifting allegiance.

The Iowa caucuses are one of the great peculiarities of American politics: a source of pride to Iowans and puzzlement to much of the rest of the country. They flout most of the basic rules of democracy. Secret ballots? Voters have to declare their allegiance at one of 1,993 public caucuses. Freedom to cast your vote for your chosen candidate? You cannot vote for anyone who gets less than 15% of the votes in the room. Voter convenience? Caucus-goers have to turn up to their caucuses no later than 6.30pm, the voting starts at 7pm, and caucuses can take much of the evening. Decent voter turn-out? In 2000, only 61,000 of Iowa's 560,000 registered Democrats turned up to the caucuses.

The state Democratic Party claims that it is doing its best to boost turnout to 100,000 this year. Most caucuses will take place in public places, such as schools, rather than in people's houses (where homeowners can influence their guests with cookies). There will be strenuous efforts to make sure that all caucus-goers are genuine Iowans; rumours have circulated that out-of-staters may try to sneak in. But even with these improvements, the United States is unlikely to try to introduce the caucus system in Iraq.

Ironically, one of the things that slowed Mr Dean's momentum in Iowa was his honesty about this circus.

Four years ago, Mr Dean told a Canadian television program that Iowa's caucuses were dominated by “special interests”, extremists and windbags. The enthusiasm with which Mr Dean's rivals—particularly Mr Gephardt—have accused him of traducing one of the jewels of American democracy has been nauseating. But Mr Dean's “clarification” of his position on the caucuses, coming as it did after several other “clarifications” on everything from Osama bin Laden to taxes, has damaged his reputation as a straight talker.

More generally, Mr Dean is succumbing to a common problem for front-runners: everybody else gangs up on you. Mr Gephardt is attacking his health-care reforms, Mr Kerry his lack of military experience. Al Sharpton was particularly effective in a Democratic debate on January 11th when he asked why Mr Dean had failed to appoint any members of racial minorities to his cabinet in Vermont.

Mr Dean has been endorsed by Seanator Tom Harkin, the most powerful Democrat in Iowa. As *The Economist* went to press, he also looked set to win the backing of Carol Moseley Braun, the only woman in the race, who was due to drop out of it. Mr Dean, who boasts that he has visited all 99 counties in his two years of campaigning in the state, expects to have 3,500 volunteers by the weekend.

Yet these Deaniacs, with their distinctive orange hats, are engaged in a pitched battle with Mr Gephardt's burly army of union workers. An unscientific survey of caucus-goers by this correspondent found plenty of them having second thoughts about Mr Dean. The most common complaint was his hot temper—an impression reinforced by his strop about not wanting to be used as a “pin cushion” any longer. But a surprising number said that they thought that he was too much like George Bush for comfort—too willing to shoot first and ask questions later.

Mr Gephardt could well gain from this. The congressman comes from neighbouring Missouri; he won the Iowa caucuses in his first run for the presidency in 1988; he has strong roots in the labour unions that dominate the state's Democratic politics; and his health-care plan panders shamelessly to the elderly people who also make up a disproportionate share of Iowa's population. Mr Dean, by contrast, appeals to younger and college-educated voters, exactly the sort of people who have been fleeing Iowa for years.

The latest Reuters/MSNBC/Zogby poll gives Mr Gephardt 21% of the vote, a mere three points behind Mr Dean. But he is only in equal second place with Senator Kerry, who also seems to have recovered his balance a little. The dark horse of the campaign, however, may well be Senator Edwards, who has risen from 5% in December to 15% and just nabbed the much-coveted endorsement of the state's main newspaper, the *Des Moines Register*.

On paper, Mr Edwards has always had plenty of strengths—not least his humble background and southern roots. This week, he addressed a group at Fair Meadows Village, a retirement home in West Des Moines: hardly the easiest audience, but Mr Edwards whipped them up into an almost youthful frenzy, eloquently condemning Mr Bush for creating two nations, with one tax system for the rich, another for ordinary Americans, one health-care system for the rich, another for ordinary Americans, and so on. If Al Gore had been able to deliver his populist message with this sort of gusto in 2000, Mr Bush would not be in the White House.

As if there were not enough problems for Mr Dean In Iowa, his main challenger may well be someone who is not even competing in the caucuses. Wesley Clark has always done well in national polls, but now the retired general is threatening Mr Dean in New Hampshire (see article). Mr Dean is sufficiently worried about Mr Clark's push to have shifted his attention from Iowa to New Hampshire at a crucial stage in the race.

All this has visibly taken a toll on him. His performance in recent debates has been faltering. Too often he has been either arrogant (as when he declared that he would balance the budget “in the sixth or seventh year of my administration”) or feeble (as with his non-response to Mr Sharpton's jibes). He has also lost his sparkle on the stump, sometimes reading a speech he must have given many times.

So the idea that Mr Dean is a shoo-in for the Democratic nomination is clearly nonsense. But for all the recent gyrations in the polls he is still by far the strongest candidate. For instance, if Mr Gephardt loses Iowa, he is effectively out of the race; even if he wins, he hardly has any money left to pay for other primary fights.

Mr Dean, by contrast, is fighting a national campaign with a national organisation: if he loses in Iowa he is still the favourite in New Hampshire, where he stands a good chance of knocking Mr Kerry out of the race. His organisation is truly impressive to behold. In Des Moines the Dean people now occupy not one

but two buildings (the second was inherited from Bob Graham's now defunct campaign). They choreograph their huge army of volunteers with military efficiency; indeed, the man responsible for the organisation, Tim Connolly, is a veteran of Desert Storm and a former Pentagon official in the Clinton administration. They watch films on a big screen TV to explain the mysterious workings of the caucus system before being assigned to precincts or phone banks. They are even setting up day-care facilities for caucus night.

Nor are Mr Dean's supporters just the children's crusade of caricature. There are large numbers of student volunteers of course—though that is hardly unusual in election campaigns—and even more people who are still fuming about the Iraq war. But there is also a smattering of trade unionists and a huge number of run-of-the-mill middle-aged people.

One group of volunteers who had driven 12 hours from Pittsburgh consisted of a thirtysomething white female college professor, a thirtysomething black lawyer and a 67-year-old retiree who had voted Republican until Mr Bush took over the party. All three listed Mr Bush's fiscal irresponsibility as a strong reason why the president should be kicked out of the White House. Mr Dean clearly has a fight on his hands, but he has built up a machine that gives him every chance of winning the war.

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About sponsorship

Ethanol

Dirty as well as dear?

Jan 15th 2004 | SHERIDAN, WYOMING
From The Economist print edition

Is the politicians' favourite fuel bad for the environment and your pocket?

Put that in your Porsche

IT'S the one topic all presidential candidates agree on in the run-up to the Iowa caucuses: ethanol production is a very good thing and should be handsomely subsidised. Forget that this grain alcohol has always been something of an economic and environmental joke. It comes from corn (or maize), which is mostly what Iowa is famous for.

The current subsidy to the industry is worth around 50 cents a gallon—or around $1.4 billion a year. The fig-leaf covering this largesse is the idea that ethanol is a clean fuel. In the 1980s, it was touted as an alternative to leaded petrol. It got another push from the 1990 Clean Air Act; to cope with the requirement for cleaner emission standards, states made the petrol industry add more oxygenates to their fuel to make it burn better. Ethanol emerged as the main such additive.

Meanwhile, the economics of ethanol production have taken a turn for the better. Efficient enzymes have led to more cost-effective fermentation, and genetically modified high-starch corn has a better yield (and so needs less processing in the plant and fewer herbicides in the field). Today there are 75 plants distilling a record 2.8 billion gallons, with a dozen more facilities under construction.

But is ethanol really that green? A debate has been stirred up by David Pimentel, an entomologist, who argues that each gallon of ethanol takes 29% more energy to make than it eventually produces. In 2002 the United States Department of Agriculture (USDA), which administers the subsidies, released a report claiming the opposite: “Corn-ethanol yields 34% more energy than it takes to produce it, including growing the corn, harvesting it, transporting it, and distilling it into ethanol.”

This might have seemed the end of the matter. But Mr Pimentel claims that the USDA study is flawed. It omits about half the inputs in corn production, including the cost of water to grow the stuff, and by using averages it avoids pointing out that some ethanol plants are extremely ungreen. It may indeed be energy-efficient to distil ethanol in eastern Minnesota, which has lots of rain and is home to the nation's cheapest corn. But in dryer Nebraska around 80% of the corn has to be irrigated, normally by natural-gas powered pumps, and much of the water comes from the fast-dropping Ogallala aquifer.

Other scientists are now trying to poke holes in Mr Pimentel's numbers. But do not expect the scientific debate about the highly subsidised crop to make a blind bit of difference to the politicians. The hand-outs for ethanol will rise again if a new energy bill goes through Congress.

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Wesley Clark

The Arkansas connection

Jan 15th 2004 | LITTLE ROCK
From The Economist print edition

A candidate finds mileage in the old Clinton magic

Reuters

The “American Son” gets a trim

BILL CLINTON, with his tolerance of homosexual soldiers and his sloppy salute, was hardly the generals' favourite when he was in the White House. Yet now Wesley Clark, the Arkansas-bred Democratic presidential hopeful, four-star general and former commander of NATO in Europe, can't seem to get enough of him. This weekend, yet another phalanx of erstwhile Clintonites is heading off to New Hampshire to campaign for Mr Clark; and insiders in Little Rock put Mr Clark's recent spurt in the polls—he is now by many measures Howard Dean's main challenger—down to Mr Clinton's people.

The general took a while to warm to the idea of cosying up to Mr Clinton. In the early days of his campaign last September, when many Friends of Bill (FOBs) jumped on board—including Bruce Lindsey, one of Mr Clinton's closest advisers, and Skip Rutherford, the president of the Clinton Presidential Foundation—Mr Clark's team tried to stay clear of them, preferring to do things its own way.

It didn't work. Mr Clark was, after all, a political novice (he couldn't even seem to make up his mind whether he supported the Iraq war); and, when his movement started to falter, it was natural to beg for help from the Clinton people.

His headquarters in Little Rock, in an old railway station, is on the street where Mr Clinton is building his $200m presidential library. Little Rock provided the setting for Mr Clinton's legendary “war room” and the 1992 winning campaign; so Mr Clark, trying to catch some of that magic, has hired several denizens of the war room, including Eli Segal and Mickey Kantor, a former United States trade representative, to steer his own effort.

Probably on their advice, Mr Clark decided to skip the Iowa caucuses and concentrate on New Hampshire. This has worked well. While the seven other Democratic candidates slug it out in the heartland, Mr Clark has managed to get more of the airwaves in New Hampshire, and is now in second place there. Besides, he has saved a lot of money.

Somebody has also been at work on Mr Clark's image. Out have gone the wordy pontifications; in has come a middle-class tax cut (sound familiar?), some direct attacks on Mr Dean, and a more aspirational air. The latest product is “American Son”, a video directed by Linda Bloodworth (the FOB who directed Mr Clinton's 1992 video, “The Man from Hope”). Some 50,000 copies have been sent to New Hampshire voters, and excerpts are being shown in campaign ads across the heartland. In one of these ads, Mr

Clinton is shown presenting Mr Clark with the Presidential Medal of Freedom for his leadership in Kosovo.

As the New Hampshire primary gets closer, ever more Clintonites are being dispatched to the state. This weekend's troop includes two former Arkansas senators, Dale Bumpers and David Pryor; James Rubin, Mr Clinton's assistant secretary of state for public affairs; Rahm Emanuel, a congressman from Illinois and a senior aide in the Clinton White House; John Dalton, a former secretary of the navy; and Mary Frances Berry, Mr Clinton's chairwoman for the civil-rights commission.

And the Clintons themselves? They have not yet endorsed a candidate, and will not do so, they say, until the Democrats have a nominee. But neither have they told their old friends to stop helping Mr Clark. Mr Segal says Mr Clinton has offered advice on polling issues and has given his thoughts on policy papers. He has also been available to the campaign “at a minute's notice”.

Hillary Clinton's position, of course, is more delicate. She cannot really want Mr Clark to win, because her putative campaign in 2008 is posited on George Bush's remaining in the White House until then. Challenging a sitting Democrat, especially one from Arkansas, can hardly be what she had in mind. On the other hand, a strong but (alas!) unsuccessful challenge by Mr Clark would keep the Clinton machinery ticking over nicely.

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Connecticut's governor

In the hot tub

Jan 15th 2004 | STAMFORD, CONNECTICUT
From The Economist print edition

But corruption in this state can be a bipartisan business

GIFTS of a new roof, kitchen cabinets and an outdoor hot tub might seem petty stuff compared with some of the things slipped into the hands of Connecticut's politicians. Yet the accusation that the state's Republican governor, John Rowland, allowed colleagues and friends to pick up the bill for work on his holiday cottage may have done him in.

On January 14th the speaker of the lower house of Connecticut's legislature announced the setting up of a committee that will recommend whether the governor should be impeached. If it says he should, and the whole house (which has a majority of Democrats) agrees, he will go before the state's Senate for trial; a two-thirds majority against him there could lead to his dismissal. Mr Rowland glumly accepts that this is a “very fair and deliberative process”. An opinion poll organised by the University of Connecticut had already found that 63% of those it asked want Mr Rowland to resign.

Allegations of petty graft have dogged Mr Rowland for years, involving, at various times, an old Ford Mustang, two fishing boats and a condominium in Washington, DC. This time things look more troubling. On November 25th, the *Hartford Courant*, a local newspaper, ran a story about the supposedly free cottage-renovation. A week later it reported that federal investigators and prosecutors had subpoenaed several of the contractors involved in the work. On December 2nd Mr Rowland said he had paid for the cottage work himself, claiming, among other things, that he had bought the hot tub at a local shop. Then, after a series of leaks from the investigators, he confessed on television on December 12th that he had made it all up.

The federal investigators appear to be interested in Mr Rowland's cottage because among those who paid for the work are several key figures in a widening federal grand-jury investigation of corruption in the state's capital, Hartford. These include Lawrence Alibozek, Mr Rowland's former deputy chief of staff, who last March pleaded guilty to taking bribes for state public-works contracts after investigators found gold coins buried in his garden; and employees of a firm owned by the Tomasso Group, a collection of construction companies which have recently won more than $100m-worth of no-bid state construction contracts (the Tomassos are family friends of the Rowlands).

Another suspect on the contract-awarding front is Peter Ellef, Mr Rowland's former chief of staff. Until his resignation in 2002, Mr Ellef also served as chairman of the state rubbish-collection authority which, under his stewardship, struck a $220m deal with Enron. This turned out to be a loan to Enron dressed up as an electricity contract, which had the effect of hiding the debt from Enron's investors.

Because the governor appoints a majority of its board, the rubbish-collection body has long been thought of in Hartford as a key component of his political machine. Yet, at the time, Mr Rowland claimed that he knew nothing about the Enron deal. After his recent admissions, that denial raises even more eyebrows. So does Mr Rowland's claimed ignorance of Mr Alibozek's dealings, as well as his earlier protestations of surprise after the discovery that Paul Silvester, Mr Rowland's former state treasurer, was taking bribes for dishing out state pension-fund management contracts. Mr Silvester is now in jail.

Until this week, Connecticut's Democrats seemed as reluctant as the local Republicans to get to grips with all this. A charitable explanation is that the governor's moderate politics had earned him support from both parties in the state. But Mr Rowland is said to have pointed out to his fellow politicians that impeachment was a danger to everyone. Richard Blumenthal, the state's (Democratic) attorney-general, admits that “favouritism and gift-giving is a deep-seated problem.” In Connecticut corruption, too, may be a bipartisan affair.

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The argument about “enemy combatants”

A few good men

Jan 15th 2004
From The Economist print edition

Allegations of “monarchical powers” at Guantánamo Bay and detainees being kept in “a legal black hole”—from an unlikely source

ONE of the many worries about the Bush administration's proposed military tribunals to try the 660 “enemy combatants” in Guantánamo Bay has been the fact that the accused have not been allowed to choose their own lawyers. The military lawyers they have been given surely would not challenge their commander-in-chief—especially not on behalf of people he has already called “bad men”.

That concern has now receded—but not for reasons that George Bush will appreciate. This week, five of the soldier-lawyers assigned to defend the first clutch of tribunal-bound detainees filed a “friend of the court” brief to the Supreme Court. According to a copy of the brief secured by the *Washington Post*, they say that the constitution “cannot countenance an open-ended presidential power with no civilian review whatsoever.” To permit this would give Mr Bush “monarchical” powers and cast the detainees into a legal “black hole”.

A Pentagon spokesman says the brief shows the lawyers' “willingness to get out there and zealously defend their clients' rights, as instructed”. They had obtained prior permission from the Pentagon's legal department. All the same, it is the first public criticism from within the armed forces.

The administration has already retreated a little on the question of civilian review. Last month, it announced the creation of a special “review panel”, composed of four civilians, to look at the military tribunals' findings. The panel will be able to order new hearings on a point of law or even dismiss the charges, but may only make recommendations to the defence secretary on all other matters, including sentencing.

The Supreme Court is examining the legal status of the American naval base at Guantánamo Bay. The administration argues that the base, leased in perpetuity from the Cuban government in 1903, is not part of United States sovereign territory. The detainees thus have no legal rights, even if they were to be tortured or summarily executed by their captors—as a government lawyer told a startled federal appeals court in San Francisco last month.

As it happens, the administration lost that case, which was brought by relatives of one of the Guantánamo detainees. The San Francisco court (a very liberal outfit) rejected the administration's claimed right to hold the Guantánamo detainees indefinitely and to hear them only before military courts, calling the procedure “counter-intuitive and undemocratic”.

The administration has also suffered reverses over two Americans it has deemed to be “enemy combatants”. In December, another federal appeals court in New York ruled that the government had no authority to detain Jose Padilla, the so-called “dirty bomber”, who was arrested in Chicago in May 2002. Meanwhile, the Supreme Court has just agreed to review the case of Yaser Hamdi, who was captured in Afghanistan in late 2001. Coincidentally, the administration suddenly agreed in December to allow Mr Hamdi access to a lawyer, the first alleged enemy combatant to be given such a “privilege”.

Civil libertarians hope that this run of small victories will eventually force the administration to treat its prisoners better. But Mr Bush's people are fighting hard. And they did win one battle this week: the Supreme Court refused to hear a case about the government's right to withhold the names and details of more than 700 foreigners who were arrested in America in the wake of September 11th.

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A job-full recovery

Just around the corner?

Jan 15th 2004 | ST LOUIS AND WASHINGTON, DC
From The Economist print edition

Jobs still haven't come back as hoped. But do not despair

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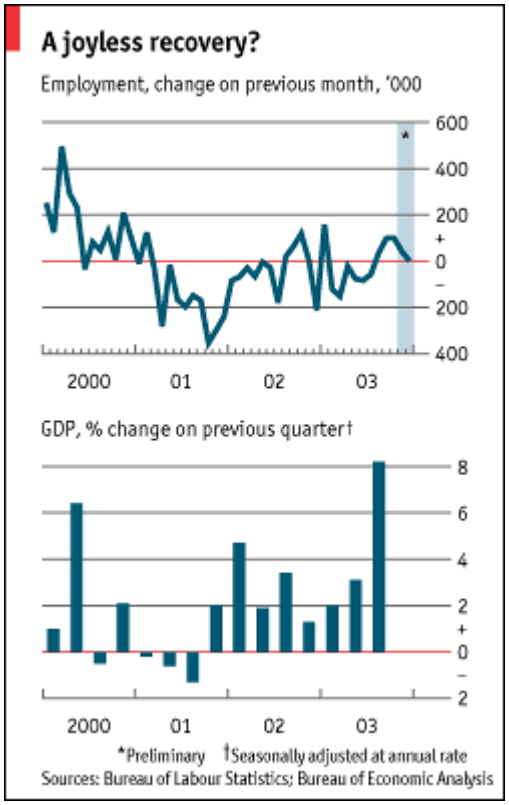

PUZZLEMENT among economists, bordering on alarm, over the economy's seeming inability to create jobs—and rare manna for Democratic presidential hopefuls. In December the economy created barely 1,000 new jobs, though something nearer 150,000 had been expected: after all, the economy grew by more than 8% in last year's third quarter, and probably by over 4% in the final quarter.

In all, over the past five months, America has generated only 278,000 jobs in non-farm businesses, a typical figure for a single month during the glorious boom. America, says Stephen Roach, chief economist at Morgan Stanley and a leading hand-wringer, is stuck in a “jobless recovery” unprecedented in scale, with no end in sight. “The ‘animal spirits' of a broad-based hiring-led revival by US businesses are all but absent,” he writes.

After America's recession in the early 1990s, it took around 15 months of economic recovery before job growth picked up—too late to help the older George Bush hold on to the presidency. This time, the economy has grown for 25 months since the (milder) recession of 2001, still with no pick-up in jobs. As a result, the younger George Bush presides over 2.3m fewer jobs than when he came to office. Nor is a fall in the unemployment rate, from 5.9% in November to a 14-month low of 5.7%, much consolation. Most of the fall was accounted for by people leaving the labour force altogether.

The figures may paint a bleaker picture than is warranted. To begin with, comparing job creation with a high point early in Mr Bush's term is probably the wrong starting-point. Unemployment then, at 4.2%, was unnaturally low; most economists think the “natural” employment rate—the rate consistent with stable inflation—is around 5.0-5.5%. As many as 1.5m jobs at the height of the boom were, in the long run, not sustainable.

Further, economists at Goldman Sachs point out that some employment weakness may be accounted for by shifting seasonal patterns of employment, notably in shops. What is more, the payroll survey from which the job figures are drawn probably misses a good deal of hiring by new firms, the kind of businesses that are often supposed to explain American dynamism. Household surveys suggest a brighter employment picture, and other measures of recovery, such as consumer confidence, are also improving.

Yet this explains away only part of the problem. Mr Roach blames “global labour arbitrage”, which, thanks to the internet and local infrastructure-development, allows not just low-paid manufacturing jobs to be sent by American businesses to cheaper places overseas, but now also upscale service-sector jobs. India is fast rivalling China as the great bugbear, because of its success in attracting information-technology and data-processing business. Senator Charles Schumer, a Democrat from New York, and Paul Craig Roberts, a former Treasury official under Ronald Reagan, wrote a piece for the *New York Times* decrying the loss of high-paying IT jobs abroad, and declaring that the laws of comparative advantage were now void.

Quite why goods or services shipped via the internet rather than by boat should not respond to notions of comparative advantage was not made clear. “Outsourcing” has been going on for decades (if not centuries), and the loss of jobs overseas did not stop the economy running at near-full employment only four years ago.

A case can be made for a less panicky view about future job growth, one that sees jobs starting to be created on the back of an accelerating economy over the next year or so. Joel Prakken, chairman of Macroeconomic Advisers, a private consultancy based in St Louis, argues that it is hardly surprising that the recovery is taking time to gather pace: the headwinds have been unprecedentedly fierce.

For a start, there was over-investment on a colossal scale in many business sectors during the previous boom. And the stockmarket bust, through the equity-wealth effect, has probably had an even greater depressant effect upon demand. The corporate-governance scandals and uncertainties after the September 11th terrorism have also helped to set back any natural recovery.

Yet now, says Mr Prakken, almost all of the earlier over-investment has been worked off; the equity-wealth effect is not far from turning positive again, thanks to rising stockmarkets last year; the country is past the worst of its corporate-governance scandals and is now more used to living with terrorism. An economy that has been growing, though below its potential of perhaps 4%, may now accelerate. After all, productivity growth has been rising, business inventories are at an extreme low and companies are making record profits. At the moment, businesses are expediently squeezing as much as they can out of their current workers, or making them work longer hours. Soon, though, they will need to hire more workers.

Mr Prakken also points out that, as part of his stimulus packages, Mr Bush instituted tax provisions that allow businesses to write off against tax a higher proportion of any capital investment they make—but it has to be done by the end of this year. This has made it relatively cheaper to spend money on machines than new people. As these incentives expire, that balance may change. Mr Roach's animal spirits may not be much in evidence; but if you listen carefully you may soon hear the herd beginning to rise from its slumber.

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Lexington

The whistle-blower

Jan 15th 2004
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Paul O'Neill's account of the White House is eccentric, but makes some painful jabs

"ANY suggestion that the White House makes decisions that are not based on sound policy reasons is baseless and groundless." Thus Ari Fleischer, then White House press secretary, in December 2002. Two hours later, John DiIulio, the former adviser who had made this monstrous suggestion, contritely admitted that his 3,000-word critique of the White House—and the article based on it in *Esquire*—had indeed been "groundless and baseless due to poorly chosen words".

Now the same charge has been resurrected, courtesy of the same *Esquire* writer, Ron Suskind. But this time it comes from a much weightier source: Paul O'Neill, the treasury secretary for the first two years of the Bush administration. Mr O'Neill gave Mr Suskind loads of treasury documents and an hour-by-hour diary of his turbulent tenure. The result is "The Price of Loyalty", published by Simon & Schuster. This time, the charge of putting politics before policy may be harder to squelch.

To be sure, Mr O'Neill is hardly Mr Reliability. He was from the start sceptical about tax cuts to stimulate the economy. This put him at odds with the White House, which is now accusing him of refighting lost battles. As treasury secretary, he is remembered for going around Africa in a funny hat with a rock star and making a series of gaffes, such as implying that America had abandoned its strong dollar policy long before it actually did. This made him the butt and despair of the administration's message-controllers. His account of economic policy is strongly influenced by his personal disdain for Larry Lindsey, Mr Bush's economic adviser, whom Mr O'Neill presents as a lightweight ideologue (Mr Lindsey was fired at the same time as Mr O'Neill).

David Frum, a former speechwriter who wrote a more flattering inside account of the Bush White House, suggests that Mr O'Neill, a former boss of Alcoa, exemplifies the dangers of the businessman in politics. Accustomed to deference, he could not accept a subordinate status. Yet Mr O'Neill was also one of the two or three most influential figures in domestic politics, so he can hardly be brushed aside. And his blunt candour, which made him such a bad politician, makes him a lively observer.

The headlines have been grabbed by Mr O'Neill's charge that Mr Bush, backed by Donald Rumsfeld, was determined to overthrow Saddam Hussein from the very start of his administration, and was therefore responsible for the war. A lot of people may believe this, but Mr O'Neill provides little evidence. Regime change in Iraq had been American policy since Bill Clinton's Iraq Liberation Act of 1998. Talking about it

in general, or proposing tougher sanctions, is very different from implementing a specific military plan. And at one point Mr O'Neill quotes Mr Rumsfeld as saying it was not his aim to get rid of Saddam.

Mr O'Neill's other big charge is that the president is guilty of a failure of leadership. Some other members of the administration—such as Colin Powell and Christine Todd Whitman (the former head of the Environmental Protection Agency)—spend a lot of time wandering around trying to guess what official policy is, since Mr Bush will not tell them. When they guess wrong, as Ms Whitman did over the Kyoto treaty, they are humiliated. Mr O'Neill says he had no idea who was really calling the shots on economic policy, but Dick Cheney seems the most likely candidate. The vice-president is presented as a sort of Madame Lafarge, stage-managing the decision to pull out of Kyoto, and pushing for the third round of tax cuts that Mr O'Neill opposed.

This failure of communication may look bad, but it is hardly unprecedented: since Eisenhower, presidents have seldom used their cabinets to make policy. By most measures, the White House under George Bush, MBA, is better run than it was under the famously disorganised Mr Clinton. Is the fact that Mr Bush sat silently in hour-long meetings with his treasury secretary, while Mr O'Neill prattled on, a sign of ignorance or of tolerance?

Arguably, Mr O'Neill's strictures reflect a clash of temperaments. Like Kent in “King Lear”, he admires impartial inquiry: he reckons his duty is to speak truth to power. Mr Bush and Mr Cheney go by a more basic code: unconditional loyalty to colleagues and the administration. Mr O'Neill's version may be more virtuous, but the latter has its uses: it encourages openness, not least in the Praetorian guard around the president.

The two fair points

Still, Mr O'Neill makes two worrying charges against the administration. The first is that it sometimes seizes on convenient “facts” without due scrutiny. He describes how a basic mistake about the federal debt ended up in the state-of-the-union address without being checked because it buttressed the case for tax cuts. This may help to explain false claims about weapons of mass destruction in Iraq. Inconvenient facts are brushed aside, which may account for the administration's extraordinary indifference to the ballooning budget deficit. “Reagan proved deficits don't matter,” says Mr Cheney. Well, we'll see.

The second is the extent to which a particular sort of politics governs the White House's actions. As a candidate, Mr Bush made a great fuss about not being as poll-obsessed as Mr Clinton. He has certainly been guilty of taking some decisions solely to win swing votes (the steel tariffs are an example). More often, his first thought is about the Republican hard core. Mr O'Neill says the White House overrode advice to toughen up legal requirements on bosses after the Enron affair because “the base was upset”. As Mr Cheney remarks about the third tax cut: “We won the mid-terms. This is our due.”

At the book's end, Mr O'Neill, reflecting on Mr DiIulio's recantation, says of the president's men: “These people are nasty, and they have a very long memory...But here's the difference [from Mr DiIulio]. I'm an old guy and I'm rich. And there's nothing they can do to hurt me.” Maybe. But he has stung them.

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Correction: Jack Ryan

Jan 15th 2004
From The Economist print edition

In "The Fitzgeralds are coming" (December 20th 2003), we wrongly identifed Jack Ryan, who is running for Senate in Illinois, as a Democrat; he is in fact a Republican

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Brazil's Indians

The Amazon's Indian wars

Jan 15th 2004 | BOA VISTA
From The Economist print edition

AFP

A battle over an Indian reservation encapsulates the arguments over whether and how to develop the Amazon

THE Amazonian state of Roraima has a whiff of impending civil strife. Earlier this month, foes of a proposed Indian reservation blocked roads leading to Boa Vista, the state's capital, and occupied the offices of the agencies for federal agrarian reform and Indian affairs. The dispute has not only polarised Roraima. It also sheds light on wider struggles between environmentalists and enthusiasts for traditional culture on one side, and advocates of economic growth on the other.

Brazil is dappled with Indian reservations. These are often vast tracts containing few people but abundant resources, from wood to gold to water. The land and what lies beneath it belong to the federal government, but the Indians control access and economic activity. Most outsiders who care about such things consider this fair. Reservations look like bulwarks against forces that might imperil both the Amazon, where the biggest ones are, and the rights of a weak minority. This view has powerful supporters, such as international NGOs and Brazil's Catholic church.

But to farmers, miners and lumbermen, this looks like a conspiracy to thwart development. Paulo Cesar Quartiero, a rice planter, says the controversial reservation in Roraima is an act of “extermination”, missing only the crematoria. Though arguments over resources can often be bloody (a score of Indian leaders are thought to have been killed last year for their wealth) they are usually local. This dispute, however, is rousing an entire state.

The trigger is the impending declaration by Brazil's president, Luiz Inácio Lula da Silva, of a new indigenous territory covering 8% of Roraima, the 1.7m-hectare (4.2m acre) Raposa/Serra do Sol. “Disintrusion” must follow. That means removing the non-Indian population of several villages and a small town—the number of people is disputed—plus several large rice plantations, Mr Quartiero's among them.

To its advocates Raposa/Serra do Sol is restoration, not expropriation. For decades, the area's 15,000 Indians have been trying to reclaim their land from miners and farmers, who brought drink, dirt and prostitution. Manuel Tavares, of FUNAI, the federal Indian agency, brandishes packages of agricultural poison that he says were found on one of the rice farms. The final cleansing will come when the

reservation is ratified.

That prospect evokes little sympathy in Boa Vista, home to over half the state's population. The local mascot is not the indigenous Brazilian but his arch-enemy, the *garimpeiro*, who polluted and mined what are now Indian lands for gold and diamonds from the 1930s to the 1980s, and now survives largely as a gold-tinted monument in Boa Vista's main square. The governor, Flamarion Portela, complains of administering a “virtual state”, where half the land is Indian and most of the rest is controlled by a federal agency. This frustrates dreams of partaking in Brazil's soyabean boom, and of exploiting road links to Venezuela, Guyana and beyond.

Boa Vista has an ethnically charged atmosphere more characteristic of the Balkans than of Brazil. “People either like Indians or hate Indians,” says Ana Paula Souto Maior, a pro-Indian lawyer. “There is no middle way.” The idea of putting parts of the state off limits to non-Indians seems unBrazilian to many.

Yet some Indians are among the most vociferous critics of the reservation in its proposed form. The reservation's supporters claim that these critics are in the pay of the rice planters, but the critics themselves say that the church and the NGOs are foisting on them a simplicity and isolation Indians no longer want. Instead they want “TVs, cars, everything”, says Gilberto Makuxi, president of Arikom, an Indian group. If Raposa goes ahead as planned, he adds, “there will be a war among us.”

The state's gravest problems are self-inflicted. Its population exploded from 41,000 in 1970 to 360,000 today. Minerals lured some, but many came for government jobs and subsidies. Half the workforce is on a government payroll. Many are being dismissed, partly because it emerged that some were hired so that politicians could skim off their salaries. This is not an economy that can shrug off the loss of the bulk of its rice farming, an industry accounting for 10% of state income.

The planters and their Indian allies want to exclude plantations, roads and settlements from becoming part of the reservation. Mr Portela hopes the federal government will turn over non-Indian federal land to the state. But that would not save Mr Quartiero's plantation. Backers of Raposa hope the fight will end once the reservation is declared. Its opponents say that is when it will really begin.

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The Summit of the Americas

Loveless brothers

Jan 15th 2004 | MONTERREY
From The Economist print edition

Making up proves hard to do

“WE ARRIVE, we greet each other, make speeches, sign a declaration, take some photos, smile, eat and go.” That was the verdict of Hugo Chávez, Venezuela's president, on this week's “special” Summit of the Americas in Monterrey, Mexico. He was not the only one left wondering why he had bothered. The summit was always unlikely to agree on anything substantial, let alone pledge eternal hemispheric brotherhood. As it turned out, the final communiqué is destined to be forgotten even quicker than most such documents, and the jamboree highlighted the subjects on which the hemisphere is divided—not least Mr Chávez himself.

George Bush, for one, did try to repair some damaged regional friendships. Widely criticised in Latin America for ignoring the region, Mr Bush came bearing gifts, especially for his erstwhile allies Mexico and Canada. For Mexico there was his guest-worker scheme—also greeted warmly by several Central American leaders. Apparently forgiven for his failure to support the Iraq war, and appreciated for his contribution to the “war on terror”, Vicente Fox, Mexico's president, even got an invitation to visit Mr Bush's Texas ranch. Then Mr Bush surprised everyone by announcing that, contrary to earlier indications, Canada would be allowed to bid for future reconstruction contracts in Iraq, despite its own misgivings about the war.

But if the northern part of the Americas seems to be making up, the summit exposed the gulf between north and south. The United States wanted trade to be a central part of the conference agenda, and a commitment to do a deal on the Free Trade Area of the Americas (FTAA) by the beginning of 2005 to be in the final communiqué. Brazil, Venezuela and others didn't want to talk about pan-American trade at all; Brazil wants to secure greater economic integration in South America first.

Eventually the attendees pledged themselves to the FTAA, but not to a specific date, and several made plain their objections to the Washington model of free trade. President Luiz Inácio Lula da Silva of Brazil dwelt on the “abyss” between the rich and the poor, and said that trade should be more “fair and equal”. Néstor Kirchner of Argentina fulminated against the International Monetary Fund for burdening his country with promises it could not keep—arguments that reflect a disenchantment with economic liberalism across South America, which has informed the rise of leaders such as Lula.

Then there was Brazil's anger at being included on America's list of countries whose citizens now have to be fingerprinted and photographed on arrival in the United States. Lula protested this indignity at a bilateral meeting with Mr Bush, and his country has retaliated by imposing extra security checks on incoming Americans (to the chagrin of many in Brazil's own tourist industry). The two countries also differed on, among other things, some aspects of a plan for tackling corruption.

The main example of hemispheric co-operation to emerge was an agreement on a multilateral initiative to nurse Bolivia's fragile democracy. To agree anything in the summit's rancorous political atmosphere was an accomplishment.

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Canadian agriculture

Better stick to celery

Jan 15th 2004 | TORONTO AND VANCOUVER
From The Economist print edition

The costly travails of Canadian farmers

Reuters

The first sign of madness

TO THOSE whom the gods wish to destroy, Canada's farmers might reflect, they first send mad cows. Eight months ago, North America's first case of mad-cow disease was found in a cow in northern Alberta. Now Canadian agriculture faces a whole haystack of separate blights.

It had seemed that the damage from the mad-cow outbreak (real name bovine spongiform encephalopathy, or BSE) might be contained. America and several other countries had reopened their borders to most cuts of Canadian beef. But hopes of a full return to normalcy were dashed by the discovery last week that America's own first BSE-infected cow had also come from a herd in Alberta.

Contaminated feed made from other animals has again been fingered as the likely culprit. The European Union banned this cannibalistic practice in 1996, but Canada and America imposed only a limited ban in 1997. Critics say the BSE crisis also reveals the inadequacy of Canada's beef-inspection system. This year's target for testing is a mere 8,000 cows, out of an annual slaughter of 3m. France and Japan test virtually every one.

Farmers have been holding back hundreds of thousands of cattle in the hope that the borders would reopen. If not, they will have little choice but to start slaughtering on a massive scale. The federal government is offering to pay C$159 ($125)—about a quarter of the pre-BSE market price, and barely enough to cover transport costs—for every old animal delivered to an abattoir before the end of the year.

How big an economic blow might BSE inflict? Unlike most other countries hit by the disease, Canada's appetite for beef remains as hearty as ever. Supermarkets are chopping prices, and the Beef Information Centre in Calgary estimates that consumption has actually risen by almost 10% in the past eight months. The federal government is helping to spread the word that Canadian beef is safe—a strategy that British ministers came to regret. In any case, estimates Derek Holt, an economist at the Royal Bank of Canada, the cattle industry, including its offshoots, makes up a modest 0.4% of Canada's GDP.

But Marvin Shauf, vice-president of the Canadian Federation of Agriculture, says the problem is that “if one person gets hit, another person feels the pain”. Already, the build-up of dairy herds has led to a milk surplus that could destabilise prices and dairy farmers' incomes. Grain farmers worry that fewer cattle will mean less demand for feed; and so on. And unfortunately for both farmers and consumers, beef is not the only worry.

New fears over farm-raised salmon have alarmed British Columbia fish-farmers (see article). Nor are vegetarians exempt, given all Canada's concerns over genetically modified (GM) foods. On January 20th, a pivotal GM case will be heard in Canada's Supreme Court. A Saskatchewan farmer is appealing a conviction for infringing a patent on GM rapeseed, arguing that the GM seed blew into his fields. Many other farmers face similar problems. Meanwhile, a row over GM wheat—not yet marketed commercially—is also brewing. The Canadian Wheat Board reckons Canada might end up losing about 80% of its annual C$4 billion international sales if GM wheat ever gets planted.

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Venezuela

Smash and grab

Jan 15th 2004 | CARACAS
From The Economist print edition

A new target for Venezuela's demagogic president

Get article background

THE otherwise sober facade of Venezuela's central bank, the BCV, is adorned with revolutionary graffiti. “A BCV for the people” and “Neoliberals out!” are two of the slogans to have appeared recently. The bank is the latest institution to be threatened with seizure by Hugo Chávez, the country's president. It is supposed to be autonomous, but the president is irked by its reluctance to do his bidding.

Mr Chávez has already persuaded the BCV to hand over the exchange-rate “earnings” accrued on the country's international reserves, as a result of the depreciation of the bolivar. Last month he also demanded $1 billion from those reserves, to subsidise agriculture. If the money isn't forthcoming by mid-January, “I'll deal with [the BCV] the same way I dealt with Petróleos de Venezuela [the state oil corporation]”. In other words: take it over.

Such a pay-out is explicitly prohibited by the BCV's regulations, as well as by Venezuela's constitution. In a statement, the bank said it was “expressly forbidden by law to grant credits to the government”. The inflationary effect of injecting $1 billion into the economy could be dire; ditto the impact on the tumbling bolivar of treating foreign reserves as if they were the government's piggy-bank. The finance ministry, in a bid to calm foreign investors, has tried to finesse the president's demands. In any case, the agricultural schemes that he says he wants to fund barely exist. Private banks, which are obliged to devote 12% of their lending to agriculture, say they have difficulty placing the money, for lack of viable projects.

But Mr Chávez himself attributes all criticism to the dreaded “neoliberals”: “I'm not interested in economic theories,” he says. Last week he claimed that the bank's reserves—currently standing at around $21 billion, thanks largely to stringent exchange controls—were $6 billion in “excess” of what the country required. It was “absurd” and “crazy” for them just to sit in a bank. The gold bars in the BCV vaults were “growing mouldy”. He insists that he will change the law, or even the constitution, if he does not get his way.

Mr Chávez's friend, Fidel Castro, once appointed Che Guevara to head the Cuban central bank: an ominous precedent. “Each day we come closer to the Cuban model,” Carlos Casanova, an opposition legislator, told parliament. One of Mr Chávez's former finance ministers, General Francisco Usón, put it more bluntly. “This is practically the same”, he said, “as showing up with a pistol...and taking the money.”

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Haiti

Blood on the streets

Jan 15th 2004 | MIAMI
From The Economist print edition

But Haiti's president remains unbowed

Get article background

AP

You're not a real student

JEAN-BERTRAND ARISTIDE says he wants to hold fresh parliamentary elections; the opposition says he stole the last vote, and won't negotiate while he remains in power—which he insists on doing until 2006. Meanwhile, the mandate of Haiti's current parliament has expired, leaving the president to rule alone. It's a familiar stalemate in a country whose history, though short, seems doomed to repeat itself.

Haiti had more than two years without a parliament in the late 1990s. This time the risks are greater. At least 40 people have already died since September in protests over alleged government corruption and constitutional and human-rights abuses. A general strike, which began last week, has shut down much of the private sector, though public employees and most of Haiti's poor, self-employed street vendors are still working. International loans must be ratified by parliament, so any further cash that the Inter-American Development Bank might have released may not arrive.

Students—the vanguard of the protests since a university campus was attacked by pro-Aristide thugs in December—demonstrated peacefully on January 12th, though a march through an area regarded as home turf by pro-Aristide street toughs, scheduled for January 15th, may be less tranquil. The president himself talks ambivalently about his critics. The students have legitimate grievances, he concedes, yet they are also political agitators: “a distinction has to be made between [real] students and false students”. Rich, coming from him: the government seems to be orchestrating the counter-protests and anti-opposition violence. On January 13th armed men wrecked the antennae of the country's main opposition radio stations.

The United States, which reinstalled Mr Aristide after he was overthrown in a coup in 1991, has criticised the handling of the protests. But Haiti's bishops may offer the best (if faint) hope of a breakthrough. In November, they proposed that parliament be replaced by a diverse interim governing council. The president accepted the idea; the opposition demurred. The Bishops Conference may take a tougher stand this weekend, perhaps insisting that Mr Aristide surrender almost all of his power.

The street clashes alone seem unlikely to dislodge him. One observer likens the protests to body-blows in a boxing match: Mr Aristide has been bloodied, but it's still not clear if or when a knock-out punch might come.

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China

Shanghai '04

Jan 15th 2004 | SHANGHAI
From The Economist print edition

ROPI

Whether you call them delusions of grandeur or visionary thinking, China's biggest city has plans that are nothing if not bold

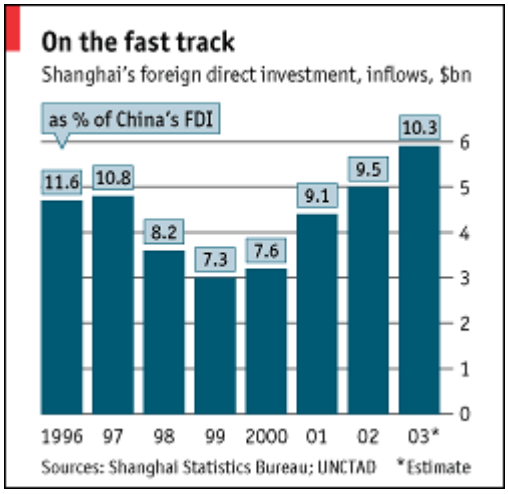
APART from a dozen Chinese tourists posing for a photograph, the platform at the oval dome-covered Longyang Road Station is nearly empty as the world's fastest train pulls in. Minutes later, with all but a handful of its 500 seats unoccupied, the train glides off, levitating on an electromagnetic cushion that propels it with barely a judder to its top speed of 430kph (267mph). It takes just eight minutes to complete the journey to Pudong International Airport, an ultra-modern structure of glass and steel 30km (19 miles) away.

Considering the thrill of being on the world's first maglev train in commercial use—and the half an hour or more saved on the journey—it might seem odd that so few people are trying it out. Since daily services were launched on December 29th, about 1,000 tickets a day have been sold on weekdays (out of 12,000 available). At weekends, when novelty-seekers are out in greater numbers, the total still only rises to about 5,000, according to Song Xiaojun, general manager of Shanghai Maglev Transportation Development Co. If the arrival of maglev is a great boon to Shanghai's overburdened transportation system, few appear to be aware of it.

It is more than just a cautious approach to rolling out this new, German-supplied, technology that is keeping numbers down. While other countries, including Germany itself, have hesitated about adopting maglev because of the high cost and uncertain returns, Shanghai has happily poured $1.2 billion into its track—even though a glance at a map immediately suggests the risks involved. Longyang Road Station, the only stop apart from the airport, is on the city's eastern fringe, a considerable distance from most residential areas. A taxi ride between the airport and Longyang costs little more than the 75 yuan ($9) price of a maglev ticket and saves the hassle of a transfer.

Shanghai's gamble on maglev, in which seven big state-owned companies have a stake, reflects an approach to the city's development that places great store on massively expensive and

commercially dicey projects. Since the early 1990s Shanghai has been driven by a desire to reclaim its pre-communist era status as a regional financial capital and a cosmopolitan haven for international capitalists eager to penetrate the Chinese market—that lavish but raffish world immortalised in Vicki Baum's novel, “Shanghai '37”. China's former prime minister, Zhu Rongji (who previously served as Shanghai's party chief and is normally known for his hard-headedness), strongly backed the maglev project when it got under way in 2000.



Cynics should perhaps beware. The city's “build it and they will come” mentality has, after all, paid off handsomely before. Many people scoffed when Shanghai announced plans in 1990 to develop what was then just an expanse of marshy land, villages and old factories into the city's new financial district. Today Pudong, as the area is called (and where the maglev is located), is a stunning conglomeration of soaring office towers and hi-tech factories (pictured above) that has attracted tens of billions of dollars in foreign investment. Last year, it is reckoned, it sucked in just under $6 billion, more than a tenth of the total for the entire country.

In the next few years, changes in Shanghai—whose GDP, according to the official figures, grew last year by a sizzling 11.8%—could be similarly dramatic. In September, the city is due to host China's first Formula One car-racing event. This has involved one of the biggest outlays of any Formula One venue in the world, with $310m being spent on a 5.5km circuit and related facilities now under construction on the western outskirts of the city.

The plan is to turn this into the centrepiece of a new “auto city” in which all aspects of the industry from manufacturing to sales will be concentrated. Yu Zhifei, deputy general manager of the track's developers, Shanghai International Circuit Co, admits that a lot of Chinese do not know what Formula One is and that many who do are sceptical about the track's ability to make money. But he says he is confident that the facility, with a seating capacity of 200,000, will turn a profit as Chinese consumers' new-found penchant for cars continues to grow apace.

The car craze is evident in the worsening congestion of Shanghai's streets. But to the maglev's operators, this is comforting. “Within a few years, it'll be very inconvenient to take the road to the airport,” enthuses Mr Song. And next year, he says, work should begin on extending the line another 7km to the site where the World Expo will be held in 2010 on the banks of the Huangpu River, much closer to the city centre. The hope is that it will become the main way to visit the fair, an event that lasts several months.

Shanghai's planners regard the World Expo as the city's greatest opportunity to show off its resurgent glory. Scepticism may abound about the ability of World Expos to generate profits. Hanover, site of the last such event in 2000, suffered a disappointing turnout. But Shanghai sees it as comparable to Beijing's hosting of the Olympic Games in 2008: an event that will fix the world's attention on the city's, and the country's, achievements. Compared to that, the $3 billion needed to build the facilities and relocate tens of thousands of residents to the outskirts is a trifle. And, anyway, by then the maglev's operators hope to be making a profit.

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India

Back from lunch

Jan 15th 2004 | DELHI
From The Economist print edition

The prime minister's stock is soaring

AFP

Vajpayee triumphant

IN THE middle of 2002 Atal Behari Vajpayee, India's prime minister, looked as though he might hobble off the world stage on ailing knees, taking his creaking body into political retirement. *Time* magazine ran a big story on how this "ordinary old man" was spending "the twilight of his political life where he wants to be—out to lunch". Nearly two years later, Mr Vajpayee still walks hesitantly on reconstructed knees, often speaks disconcertingly slowly, and enjoys his lunch more than he perhaps should at 79. But he is increasingly recognised as one of the world's most surprising statesmen. Now he is pushing his Bharatiya Janata Party's (BJP) multi-party coalition into an early general election, confident of a victory that few analysts are yet prepared to question.

In the past fortnight Mr Vajpayee has pulled off a reconciliation with President Pervez Musharraf of Pakistan, setting the two countries on the most promising, if uncertain, path to peace for years. He persuaded President George Bush to announce, on January 12th, a long-awaited co-operation agreement in high technology, space and nuclear products, which will beef up India-American relations. He got Jaswant Singh, his finance minister, to produce not one but two generous pre-election mini-budgets on January 8th and 9th. And L.K. Advani, his deputy prime minister, is to back up planned talks between India and Pakistan by meeting leaders from Kashmir's separatist All-Party Hurriyat Conference on January 22nd for their first-ever formal talks on devolution.

Mr Vajpayee also seems energised by the prospect of the election campaign. At a recent political rally he spoke with the sort of force and clarity that once made him famous as an orator, and said he hoped a new government would be in place by the end of April.

The prime minister's 2002 low point came when more than 2,000 people were killed in Hindu-Muslim riots in Gujarat. Afterwards, the state's controversial chief minister, Narendra Modi, won a landslide assembly victory for the BJP on an anti-Muslim ticket. That strengthened hardliners within the Sangh Parivar, the Hindu "family of organisations" to which the BJP belongs, and led to fears of similarly provocative election campaigning elsewhere. But, following a defeat in a small northern state, Mr Vajpayee tacked to a more moderate line, with campaigns stressing development and stable government. He was rewarded in December with election victories in three key states.

Mr Vajpayee now seems unlikely to retire before his health compels him to, and certainly not, as was mooted a year or so ago, soon after the coming election. "If he works at 79, he can work at 84," says Pramod Mahajan, a prominent BJP politician. That seems to be accepted by the 76-year-old Mr Advani, who has long been a rival as well as an ally, and whose prospects of becoming prime minister fade the longer Mr Vajpayee remains. Mr Advani is seen as a nationalist hardliner. He cannot mount a challenge now because he knows that he would find it difficult to hold the BJP's National Democratic Alliance coalition together, let alone win an election, if Mr Vajpayee were to depart.

The BJP's election confidence stems partly from disarray in Congress, the main opposition party, which is ineptly led by the Italian-born Sonia Gandhi, widow of Rajiv Gandhi, the former prime minister assassinated in 1991. The BJP plans to campaign on a strong economy (with growth of over 7% last year), stable government and now the prospect of peace with Pakistan. It adds up to a hard act to beat.

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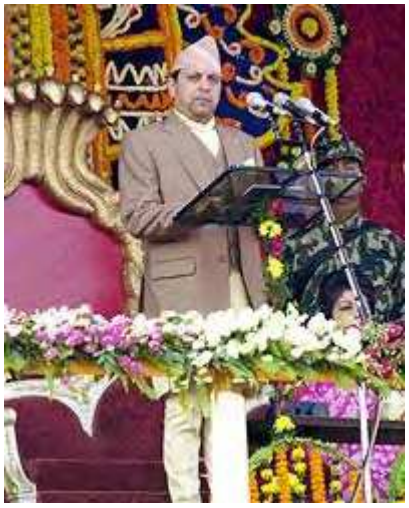
Nepal

King and country

Jan 15th 2004 | KATMANDU
From The Economist print edition

Is the monarchy doomed?

AP



Still reigning

THE two pillars of the modern Nepali state are in big trouble. Parliamentary democracy, the first, is in limbo after King Gyanendra dismissed the most recent elected government 15 months ago. Now the second, constitutional monarchy, is under threat from a growing republican movement.

For weeks now, students chanting anti-king slogans have clashed daily with the security forces in the streets of the capital, Katmandu. There have been hundreds of arrests, but the rioters' wrath shows no signs of abating. The students' republicanism might once have been dismissed as youthful extremism, like that of Maoist rebel guerrillas who have been fighting for eight years in the countryside for a “people's republic”. But lately, senior leaders of democratic political parties have been edging towards the students' and the Maoists' point of view. This includes political centrists who helped negotiate the transition from absolute to constitutional monarchy after pro-democracy riots in 1990.

Questioning the monarchy was once unthinkable in Nepal, even after the country adopted democracy. The then king, Birendra, was a much loved figure, above the rough and tumble of Nepal's tumultuous politics. Everything changed after the infamous royal massacre of June 2001. Official reports and eyewitnesses said the Crown Prince Dipendra—crazed by drugs, alcohol and his love for a woman rejected by his parents—gunned down most of his close family, at a dinner party, before killing himself. King Gyanendra, who was absent from the scene of the massacre, ascended the throne and was initially admired for his quiet dignity.

The king's dismissal of the admittedly corrupt and incompetent government of Sher Bahadur Deuba in October 2002 was not an unpopular move at first. Many blamed politicians for the country's troubles. But it soon became clear that King Gyanendra had assumed executive authority himself, a move that many say is illegal. “When a constitutional monarch defies the constitution, then one of them has to go,” says a pro-republican lawyer. Two governments picked by the king have fared no better at resolving Nepal's problems.

Also, the return to civil war with the Maoists last September, after seven months of peace talks, is blamed on hard-line royalists who convinced King Gyanendra that the rebels could be defeated in battle. That decision cost hundreds of lives and led to a steep erosion of civil liberties. Still, the king has some aces up his sleeve. He is backed by the powerful Royal Nepalese Army. Nor are his opponents saying what form any future republic might take. Nepalis may be growing restless with monarchy, but the return of discredited, corrupt democrats is not met with much enthusiasm either. Then there are the Maoists. Their demand for a communist republic is chilling to most people in the country. Monarchy is down in Nepal. But it is not yet out.

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About sponsorship

Thailand

Trouble down south

Jan 15th 2004 | NARATHIWAT
From The Economist print edition

Al-Qaeda or arms smugglers?

BOMBS, arson, banditry, murder—the residents of the four Muslim-majority provinces of southern Thailand have seen plenty of these over several decades of separatist agitation, but never all at the same time. Until now. Over the past two weeks, unknown assailants have burned 21 schools, stormed a military base and stolen the guns in its arsenal, shot up a police station, assassinated an army informant and planted several bombs, killing seven people in all. In response, Thaksin Shinawatra, Thailand's prime minister, has extended the scope of an existing martial-law decree, and sent his top soldiers and security officials to the area with instructions not to return until the culprits are caught.

In fact, Mr Thaksin himself bears some responsibility for the chaos. Violence attributed to southerners wanting to secede from largely Buddhist Thailand and join their fellow Muslims in Malaysia had been dwindling, so much so that Mr Thaksin declared the insurgency at an end in 2002, then abolished the joint command of soldiers and police designed to tackle it and shuffled the local army commanders several times. The number of violent incidents has been rising steadily since.

In the meantime, preparedness obviously suffered. The army apparently had no inkling of the recent wave of co-ordinated attacks, involving some 100 people, and left only four soldiers to guard an arsenal of more than 100 weapons. Even afterwards, local policemen could still be seen whiling away the afternoons sipping tea.

Grander officials on the scene, doubtless hoping to cut short their stay in the sticks, are now coming up with all sorts of pat explanations for the violence. Some say the attackers are apolitical arms smugglers, seeking to settle scores and replenish their stocks. Others blame separatist terrorists, inspired, if not directly abetted, by groups such as al-Qaeda and Jemaah Islamiah. The true culprits, according to Panitan Wattnayagorn, an academic, lie somewhere between the two: a hodge-podge of separatists, Islamic militants, and criminals with more than one reason to make mischief. It was co-operation among these disparate groups, he argues, that allowed them to mount a relatively complicated and sweeping offensive.

Yet locals, at any rate, do not seem unduly concerned. That is in part because the mysterious assailants mainly target symbols of government authority, particularly military bases. What's more, there is little sign of tension between local Muslims and Buddhists. Wan Muhammad Nor Matha, the interior minister, is himself a southern Muslim, and has promised to respect local sensibilities while tracking down the troublemakers.

But in the long run, the unrest will not be solved by security measures alone. People in Narathiwat province have three and a half years less schooling, on average, than residents of Bangkok, and earn scarcely one-eighth as much. No wonder Mr Thaksin recently promised to bring prosperity to the region, much as he and his predecessors have long promised to bring peace.

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Drug addiction in Afghanistan

Demand-driven

Jan 15th 2004 | KABUL
From The Economist print edition

Returnees are bringing bad habits with them

QUIVERING with heroin craving, Asadullah stabs at his withered arms with a loaded syringe, prospecting for a vein. He closes his eyes, and wiggles the needle under his skin. After 40 minutes, he finds a vein and sighs as the opiate enters him. As his veins collapse, these daily infusions are getting harder for Asadullah, one of Afghanistan's thousands of new heroin addicts. Soon, he says, he will have to start injecting his testicles.

Afghanistan has been the world's biggest opium producer for over a decade, but until recently had surprisingly few addicts. Two factors have wrought the change. Since the fall of the Taliban two years ago, 3m refugees have returned home from Iran and Pakistan, including thousands of addicts. Second, Afghanistan's drug barons have become more sophisticated, refining more opium into heroin. According to a recent estimate, Afghanistan may suddenly have gained 1m habitual drug users, equivalent to 4% of the population.

Refugee life lent itself to drug abuse. Afghanistan's 23 years of war, against the Soviet Union and then between Afghans, gave many fugitives sorrows to forget. Supply, of course, was no problem. Pakistan and Iran, along with the former Soviet Central Asian countries, consume around 90% of Afghan opium. To pay for his habit, Asadullah found work in the construction industry. Since returning to Kabul three months ago, he has been jobless. Now he has $80 left to support his $4 a day habit.

Asadullah said he would do anything to be off heroin, but his prospects for this look dim. The Nejat Centre in Kabul is the country's only one for drug rehabilitation. It has ten beds for male addicts, and offers out-patient counselling for women. According to one doctor, 70% of the clinic's in-patients are weaned off drugs through a combination of counselling and medicine: an unusually high success rate. But though medical drugs are in short supply, narcotics are not. Over the past two years, Afghanistan's government has exercised little control outside Kabul, and opium production has soared. Last year's crop earned Afghan opium farmers and traffickers $2.3 billion, or around 50% of GDP. This year's harvest, due in April, is expected to be the biggest in the country's history. A dozen heroin factories were dismantled last year, including one in the back garden of a provincial police chief. A dozen caches of acetic anhydride, a chemical whose only plausible use is to turn opium into heroin, were also seized. Production continues anyway. Kabul's heroin addicts have no trouble getting a fix. According to Asadullah, the local heroin is of poorer quality than he was used to in Iran. But it is much cheaper.

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Japan

The shock of the comparative

Jan 15th 2004 | TOKYO
From The Economist print edition

Now for the bad news

IN A country where harmony is prized, direct criticism, even the constructive kind, is still often unacceptable. Though the Japanese love to rank things—witness the popularity of television shows that count down the top 100 *ramen* (noodle) shops—these light-hearted shows rarely say anything derogatory.

But Japan is changing. It started when foreign financial ratings agencies came to town. Their harsh analysis proved much more useful to investors than the uncritical reviews published by their Japanese counterparts. Restaurants, too, were used to guidebooks filled with glossy pictures and affable descriptions, rather than critiques of their fare. Zagat, a global surveyor of restaurants, changed that in 1999 when it launched its guide to restaurants in Tokyo, complete with its trademark numerical ratings and caustic comments. Its local publisher says that disgruntled restaurants seem readier to complain about the reviews they receive than to respond by improving their fare.

Hospitals, long pampered by policies that discourage competition, are nowadays also beginning to find out what people really think of them. Though doctors are revered in Japan, a stream of scandals, including a recent one in which three inexperienced physicians were charged with killing a patient by performing complex surgery with the help of an instruction manual, have created public distrust.

That prompted Oricon, a company that publishes Japan's weekly pop-music charts, to rank hospitals as well. Last August it published a book in which 1,502 medical institutions in the Tokyo area are rated by their patients, rather than by doctors or experts.

Universities in Japan are used to being ranked by their academic prowess. Now their finances are being ranked as well. This month S&P, an international ratings agency, published its first ratings of the creditworthiness of universities. These institutions face fierce competition in coming years, as a falling birth rate produces too few applicants for too many places. Good ratings should help to reassure applicants that the university they choose will be able to survive.

In moaning about poor reviews instead of improving performance, Japan's restaurants, hospitals and universities are merely following the example of their government. Japan's own credit rating has slipped several notches in recent years, as growth has stagnated and government debt has ballooned. Instead of raising its game, the finance ministry habitually lashes out at the bearers of bad news.

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The Philippines

Mrs Arroyo's compassion

Jan 15th 2004 | MANILA
From The Economist print edition

Or how to get rid of a problem

BARRING any hitches, Joseph Estrada plans to leave the Philippines on or around January 23rd, after the court where the former president is on trial for his life for corruption gave him permission to have medical treatment in the United States. The prosecution believes he will never return, and the government sounds positively eager to get rid of him. If Mr Estrada absconds, President Gloria Arroyo will be rid of an impediment to her efforts to win the presidential election in May. But the Philippines will be left with its reputation as a country where those accused of corruption rarely face justice.

Mr Estrada's doctors told the anti-corruption court that their 66-year-old patient needed knee surgery, supposedly unavailable in the Philippines, to prevent him from being paralysed. The judges ordered him to deposit a bond for 1m pesos ($18,350) to pay for four policemen to escort him in America, and to return by March 31st. The prosecution said it would appeal against the decision to the Supreme Court, if necessary.

President Arroyo's spokesman said the decision was purely judicial. But there is little doubt that the judges took note of the president's public statement that Mr Estrada should be treated with “humanitarian compassion”. Moreover, the government made special efforts to provide Mr Estrada with a passport. And when America appeared reluctant to give him a visa, the government said it would put in a good word for him.

Mr Estrada was deposed by a popular uprising in January 2001, after being accused of misappropriating some 4 billion pesos. Mrs Arroyo, then vice-president, replaced him. Mr Estrada was later arrested and has since been held in detention while he is tried for “economic plunder”, a crime punishable by death.

He denies any wrongdoing. Soon after his arrest, thousands of Mr Estrada's supporters rioted outside the presidential palace, in what Mrs Arroyo's government described as a rebellion. Last year, some 300 servicemen mutinied. The government described the mutiny as an attempted coup meant to return Mr Estrada to power. Once Mr Estrada is abroad, Mrs Arroyo would surely not mind if he never returned. Although he is a spent force, his supporters are not.

One of Mrs Arroyo's strongest challengers in the coming presidential election is Fernando Poe. Mr Poe is a close friend of Mr Estrada. Both were popular film actors, and both appeal to the same constituency among the two-fifths of the population that live in poverty in the Philippines. Freedom for the ex-president is expected to diminish the Estrada-Poe constituency's rancour against Mrs Arroyo, and weaken Mr Poe's electoral support.

The price Mrs Arroyo would have to pay is reduced credibility. She asserts that she is a reforming president, intent on changing her country's corrupt old ways. Since taking office, she has repeatedly stated her belief in the rule of law. The court's decision to allow Mr Estrada to go abroad may follow the letter of the law. But the country's adherence to the spirit of it must remain in doubt as long as Mrs Arroyo appears so eager to give such a celebrated suspect such an easy opportunity to escape justice.

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Tasmania

Van Diemen's reborn land

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The convicts would be astonished

Get article background

THE island has always been burdened by its past. Under its old name, Van Diemen's Land, it was notorious as Australia's most violent British colony, a place where convicts were brutalised and aborigines hunted down. That savage history haunted Tasmania long after it was renamed in 1856. Its isolation and conservatism did not help. After the rest of Australia had decriminalised homosexuality, for instance, Tasmanian authorities in the late 1980s were arresting gay activists. As the rest of Australia boomed in the 1990s, Tasmania grew poorer. Five years ago, its population (476,000, about 2.5% of Australia's total) started falling for the first time in 50 years. Tasmania jokes were popular in the more sophisticated mainland cities of Melbourne and Sydney.

Many of the jeerers are now flocking to visit. Tourism is soaring, the economy is growing (the forecast is 3.5% next year), unemployment is falling and Tasmanians are no longer leaving home. The revolution in the island's fortunes seems to have started about two years ago, after September 11th. The terrorist attack in Bali that killed many Australians, and the SARS respiratory infection in Asia, also persuaded many Australians to holiday at home. Those who ventured to Tasmania found an island almost locked in time, with clean air and charming waterfront houses selling for a fraction of rocketing property prices on mainland Australia.

A property boom followed, with prices doubling in some areas in less than a year. Real-estate agents say that about 40% of buyers are middle-aged mainlanders, relocating to Tasmania or investing for the future. A record 700,000 people visited last year. Cheaper air fares, following a shakeout in Australia's airline industry, and the introduction of two daily ferry services from Melbourne in 2002, have fed the rush. A third ferry, from Sydney, started operating on January 13th.

Political forces have also been at work. Jim Bacon, a former union official, who led a state Labor Party government to power six years ago, says modernising Tasmania's image was crucial in order to rebuild its economy. Last year his government brought in a law, which Mr Bacon argues is the most progressive in Australia, legally recognising gay relationships. Rodney Croome, a gay-rights activist, agrees. “Tasmania was an embarrassment,” he says. “Our old image affected our reputation and economy. People stopped visiting and buying our products.”

Mr Bacon made another bid for the headlines last year with his appointment of Richard Butler, an Australian who once headed the UN's arms inspectors in Iraq, as Tasmania's governor, the nominal representative of the British monarch. By choosing an avowed republican from Sydney, Tasmania has gone further than any other Australian state in modernising this anachronistic constitutional position. Mr Bacon hopes that Mr Butler's reputation will also attract foreign investment.

Even so, Mr Bacon's new Tasmania still has image problems. As his government sets out to sell the state as one of the world's last pristine environments, it is beset by controversy over its policy of chopping down old forests. Greens say that one of the latest victims last month was the world's biggest flowering hardwood tree in Tasmania's Florentine Valley. It was apparently felled by accident. Mr Bacon counters that logging is an irreplaceable part of the economy, and points out that 40% of the island's forests are

already protected. Under pressure from environmentalists, he recently promised to phase out the felling of old forests by 2010. His critics say few old trees may be left by then.

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The Middle East after the Iraq war

Is a Pax Americana in the offing?

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Despite the misery of Israel-Palestine and the bloody uncertainty in Iraq, there are hopeful signs across the wider region

“THERE is no longer any place for dictatorship,” said the president. “Democracy is the choice of the modern age for all peoples.” Was this George Bush, preaching reform to Arab leaders? No, it was one of those leaders themselves, Yemen's Ali Abdullah Saleh, addressing a recent human-rights conference. Apart from blasts at Israel and demands for a swift American exit from Iraq, Mr Saleh's speech might have been scripted in Washington.

In the wake of the Iraq war, many Arabs still think of America as a bully. Fully 94% of 1,600 callers-in to a recent debate shown on the al-Jazeera satellite channel agreed with the proposition that America is engaged in a “crusade” against Islam. Yet Mr Saleh is not alone among Arab leaders in finding it politic to endorse, in words at least, the agenda for reform that the superpower has sketched for the region.

The changes do not mean that dictators are falling like dominoes, as some of the cheerleaders for America's invasion of Iraq were prophesying last year. But nor has the region seen the mayhem predicted by many of the war's opponents. Some of the changes have nothing to do with the war: in many countries, moves to widen political participation, liberalise commerce and contain conflicts have been under way for some time.

The so-called “Arab system”, institutionalised in the Arab League whose yearning for a place on the world stage occasionally grated with America, has been crumbling since the shock of Saddam Hussein's invasion of Kuwait in 1990. And many Arab regimes have long been zealous in pursuit of one big American objective, to exterminate terrorism (except, of course, when it is Palestinian).

But the pace of change has accelerated in recent months, with some noted gains for American policy. With much American cajoling, for example, the Sudanese government and southern rebels look close to agreeing to end that country's long civil war, so helping to calm the troubled Horn of Africa for the first time in a generation. Libya and Iran have both opted to expose their nuclear programmes to outside monitoring, and so helped to reduce the potential for a regional arms race. And Iran, while shying from any formal embrace with America (see article), is quietly courting America's close friends in the region, such as Kuwait, Jordan, Saudi Arabia and Egypt.

In North Africa, Algeria remains shaky and violent, the three-decade-old Western Sahara conflict continues to fester, and both Tunisia and Egypt still fake democracy while stifling dissent. Yet all the countries in the region, including now Libya, openly back such American aims as reducing trade barriers, while quietly offering help against al-Qaeda to the Pentagon and CIA. Egypt's gutter press hectors as loudly as in the days when it was bankrolled by Mr Hussein, but in recent months the more dominant state-owned media have muted their routine bashing of America.

Long-time American protectorates, such as Jordan and the smaller Gulf monarchies have moved more boldly to please their patron. None is near to becoming a full-fledged democracy, but all have embarked on more liberal paths. After a decade of virtual legislative standstill, for example, Kuwait's government is promoting educational reform, a redrawing of electoral districts to make voting fairer, and a removal of barriers to foreign investment.

Even Saudi Arabia is in the throes of change. Despite the fact that America's imprimatur raises hackles among conservatives, the kind of policies that American diplomats have urged for years are now firmly on the agenda. These include a widening of the franchise through promised local elections, the opening of the upstream oil sector to foreign firms, purging the state curriculum of incitement against non-Muslims, and recognising the Shia minority's rights. The reforms have been applied hesitantly, unevenly and inefficiently, but the resisters to change are now, for the first time, on the defensive. In one area, at least, the Saudi government is acting firmly, to America's pleasure, with an all-out assault on Islamic militants.

Not yet a Damascene conversion

Syria is the region's one country that still seems to resist American pressure. Yet this may simply reflect its bigger legacy of bad blood with the superpower; its isolated rulers may feel they have more to lose by knuckling under. Nor have the Americans hinted at what Syria might gain (apart from not being clobbered in its turn) by obeying their orders to abandon chemical weapons, allow greater freedom, withdraw its army from Lebanon and end support for the Hizbullah fighters there.

Having recognised their serious miscalculation in predicting that Iraq would prove another Vietnam, however, Syria's rulers seem to be looking for ways to placate the superpower. President Bashar Assad has made overtures to Turkey, a key American ally and long-time foe of Syria, and has also said he wants to talk peace with Israel. Mutual loathing, Mr Assad's precarious internal position, and the reluctance of Israel's government to make territorial concessions all conspire to make Syrian-Israeli peace unlikely any time soon, yet even the start of a process would do much to soothe the region's nerves.

Oddly enough, those that have done the least to please America are its closest Middle Eastern ally, Israel, and the feeblest of its regimes, the Palestinian Authority. This time last year, the American administration was soothing Arab anxiety over the looming war in Iraq with promises that America's victory would be followed by a huge push for Palestinian-Israeli peace. Mr Bush did announce a plan. But neither side has yet begun to implement it, and the Americans, for the time being, are no longer pushing at all hard.

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The Palestinians

Whose is their voice?

Jan 15th 2004 | EAST JERUSALEM
From The Economist print edition

Palestinian hardliners are gaining ground

THE killings go on and the political stalemate persists. On Christmas Day, Israel carried out its first "targeted" assassination in two months, killing two Islamic Jihad men and three civilians in Gaza. Hours later a Palestinian bomber killed himself and three Israeli civilians in Tel Aviv. In reprisal, Israel's army mounted an incursion into the West Bank city of Nablus that killed one Palestinian and wounded 17 others. On January 14th a Palestinian suicide bomber killed herself and four Israelis (three of them soldiers) at a crossing between Israel and the Gaza Strip.

Israel's prime minister, Ariel Sharon, has served notice that, unless the Palestinian Authority (PA) cracked down on Muslim fundamentalist groups like Hamas and Islamic Jihad, Israel would "disengage" by seeking to enforce its own solution in the occupied territories, with a security wall carving through the West Bank and threatening to slice Palestine into three enclaves on about half the West Bank's land. Gaza would be a disconnected fourth chunk. On January 11th Mr Sharon's promise to dismantle some Jewish settlements as part of this plan provoked a furious demonstration by 100,000-plus settlers and their sympathisers in Tel Aviv's Rabin Square.

The PA's dwindling hope is the "road map" proclaimed with much fanfare by President George Bush last June but which, by August, had withered as the violence goes on. The map proposed that Israel would withdraw from the West Bank cities it reoccupied after the latest *intifada* and freeze Jewish settlement. The Palestinians were to cease fire and disarm their militias. But their newish prime minister, Ahmed Qurei, has yet to get anywhere near doing that.

Early last month, Egyptian-mediated ceasefire talks between the Palestinian factions broke down. The Islamists said they would stop attacking civilians inside Israel only if Israel guaranteed to end its assassinations and incursions in the occupied territories. Mr Sharon said he could not. Mr Qurei has refused to meet his Israeli counterpart because, so long as he is unable to persuade the Palestinian factions to cease fire, he has nothing to trade.

Even if he could fix a truce, he may be losing the power to police one. The PA shows signs of disintegration, with cracks not so much between the more secular Palestinians and the Islamist opposition as between the PA's own governing institutions and Yasser Arafat's Fatah movement.

In November, Palestinian gunmen, quite likely from Fatah, tried to kill Ghassan Shakaa, the mayor of Nablus, a scion of one of the district's big landowning families and a long-time champion of their interests over the younger and poorer Fatah rebels who now rule the refugee camps. Elsewhere in the West Bank and Gaza, Fatah fighters have laid siege to PA police stations, demanding jobs and money as the price of any ceasefire.

Amid this chaos, Hamas looks like a paragon of discipline. It has claimed no suicide attacks inside Israel since September, notwithstanding this week's suicide bomb at a border checkpoint and the mortars with which its militias pepper Jewish settlements in Gaza every day. Hamas may, for the moment, be exploiting Fatah's disarray to make political headway within the PA's areas rather than to fight the Israelis. This mutual enmity eases among the foot-soldiers, hence a joint claim of responsibility by Hamas and the al-Aqsa Martyrs' Brigade, an armed wing of Fatah, for this week's suicide bomb.

Islamists from Hamas and Islamic Jihad recently won an absolute majority in elections for the student council at the West Bank's Birzeit University, once a bastion of Palestinian secular nationalism. Similar Islamist coalitions now control most of the Palestinian universities, together with influential professional bodies such as the Engineers' Association in Gaza. This bolsters the findings of most pollsters: that if

there were a freely contested general election in the PA, Hamas would not only reach parity with Fatah in most areas but, in some, such as Gaza, Hebron and Nablus, it might well eclipse its rival.

So Mr Sharon's plan to disengage also holds much less dread for Hamas and Islamic Jihad than for the Palestinian nationalists of Fatah, who favour a two-state solution based on Israel's full withdrawal from the territories it captured in 1967. The Islamists have long viewed the “armed *intifada*” as a means to force an Israeli withdrawal rather than negotiate one. A unilateral Israeli retreat from half the West Bank and parts of Gaza would, in their eyes, simply keep the flame of the conflict alive.

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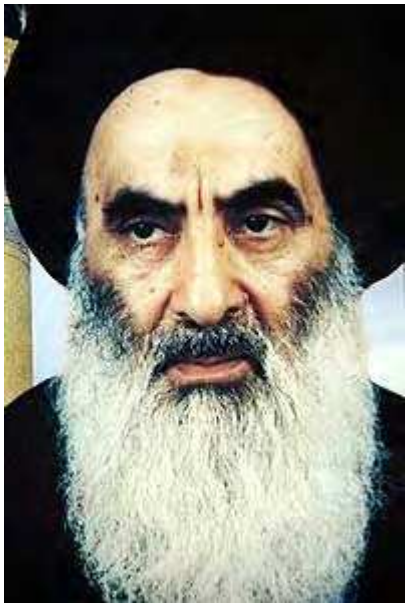
Iraq's Ayatollah Ali Sistani

The stubborn sage of Najaf

Jan 15th 2004 | BAGHDAD
From The Economist print edition

Can the latest dangerous political deadlock be broken?

AFP



THE Americans are becoming exasperated by Iraq's most powerful ayatollah. Last November, they bowed to the country's top Shia cleric, Ali Sistani, after he insisted that the new constitution be drafted by elected representatives and not American nominees. Now he is demanding that the assembly due to choose a government to start ruling Iraq in July should also be directly elected rather than selected by caucuses chosen largely by the Americans' own Iraqi appointees. If the Americans bow, once again, to Mr Sistani's demands, that might enrage Iraq's Kurds and Sunni Arabs. But if they rebuff the ayatollah, they might tip the country's largely pro-invasion Shias, who count for 60% of Iraqis, into opposition.

The Americans say it is technically impossible to hold a fair election by May, when the assembly is supposed to take shape. Moreover, they fear that if they did have a rough-and-ready poll in the summer, as Mr Sistani demands, they might lose control of a country into which American taxpayers are pouring at least $18.6 billion for reconstruction and which has already cost 500-plus American lives.

Yet without the ayatollah's nod, the plans of Paul Bremer, Iraq's American proconsul, to hand the government over to Iraqis could be scotched. The grand ayatollah commands as much loyalty among the country's Shia Muslim majority as the pope does among Catholics, so it is up to him whether the Shias boycott the political system being set up by the Americans or, even more drastically, whether they join those among the disgruntled Sunni Arab minority who violently oppose the Americans and their allies. Tens of thousands of Shias demonstrated this week in Basra in favour of his election call.

One big snag is that the ayatollah, who has secluded himself for the past decade in the Shias' holiest city, Najaf, refuses to grant Mr Bremer an audience. So the proconsul has had to rely on the 25-strong American-appointed Governing Council, which embraces representatives from across Iraq's sectarian spectrum and has believed for months that it could persuade Mr Sistani to accept an indirect form of election to the transitional government. This week, however, he seemed to rule out the possibility of backing down by issuing a *fatwa* insisting that “every Iraqi must have the right to vote”. But Adnan Pachachi, a former foreign minister now on the Governing Council, said he still thought that Mr Sistani would compromise.

The Americans, aghast at the prospect of a mullah setting the political agenda, had hoped to twist his arm. Last year they faced down Muqtada al-Sadr, a firebrand cleric who claimed to speak for the Shias' urban poor. Mr Sistani, they reprovingly note, is an Iranian whose Arabic is heavily accented. Moreover, since he and other top Shias were kept out of the public arena in Saddam Hussein's era, he is a political novice. What is more, say the Americans, Shias are loyal not just to their religious figures; they also pay homage to tribal sheikhs, who may be readier to accept patronage and power from the Americans.

Yet if Mr Bremer once again defers to the ayatollah he risks alienating many of America's other, increasingly nervous, Iraqi allies. Iraq's Kurdish leaders, who have recently become more vociferous in demanding autonomy, fearing they would lose influence if the transitional government were directly elected. Some Sunni Arabs and Baathists, who are now sidelined, think that direct elections might bring them back into the fold—a wretched prospect for the Iraqis inside the Americans' circle of power, especially the former exiles who make up the bulk of the Governing Council. Even the Supreme Council

for Islamic Revolution in Iraq (SCIRI), the Shia party that claims to be closest to Mr Sistani, had assured the Americans that he would not force them to tear up the timetable they had heralded, apparently with wide Iraqi acquiescence, in November.

Some think a compromise could still be struck, just. The ayatollah says he would accept the verdict of the UN, if it chose to return to Iraq. But he apparently fears that the Americans and British would lean on Kofi Annan, the UN's secretary-general, to declare that the continuing violence in Iraq made it impossible to take a census and produce an electoral roll within the six-month timeframe. Mr Sistani, however, says that ration cards used to administer the UN's oil-for-food programme in Iraq could serve as voters' registration cards. This month new ration cards replacing the ones that expired at the end of last year were issued without many hitches.

Mr Bremer is now looking at an “outreach programme” to make the caucuses more open, in a last-ditch bid to win Mr Sistani's approval. But time is short. By the end of February the proconsul must pass a “fundamental law” spelling out how the transitional assembly should be chosen.

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Land reform in South Africa

More squeeze than grab

Jan 15th 2004 | JOHANNESBURG
From The Economist print edition

Don't expect Zimbabwe-style land invasions in South Africa

URGED on by populist politicians, thousands of squatters congregated on a white-owned farm. A car drew up, overloaded with sticks and scrap, which some of the squatters used to start building a makeshift house. “Why this land? It is the only place we have got,” said one. Police and two cabinet ministers stood and watched. Zimbabwe? No, South Africa.

That scene, which took place near Johannesburg two years ago, is just the sort of thing white South Africans dread: that their property may be grabbed, as white Zimbabweans' land has been. But such fears are overstated. Unlike in Zimbabwe, the law counts for something in South Africa. After a court ruled that those squatters had acted illegally, bailiffs forced them out. Shacks and shebeens were piled on to trucks and removed; the fields they occupied are now being farmed again.

But still, some whites are not reassured. The reason: Thabo Mbeki, South Africa's president, is poised to sign an amendment to a 1994 land act to let his minister of agriculture expropriate farms without going to court. This will only be allowed in cases where black South Africans can show that the land was once theirs, and that it was unfairly seized. The law also says that the existing owner must be fully compensated. But farmers and the opposition are predicting havoc. “Mbeki set to back land grabs,” blared one headline.

Loose talk by ruling-party politicians lends credence to such dire forecasts. South Africa's foreign minister calls criticism of Zimbabwe's land invasions “unrevolutionary”. Mr Mbeki has opined that forcible grabs were “perhaps inevitable” in Zimbabwe when peaceful land reform failed. No wonder some South African farmers are anxious.

“We have no certainty that a Zimbabwe situation will not happen in South Africa,” says Wilhelm Auret of AgriSA, a farmers' union. He notes that some 1,500 farmers and their relations have been murdered since 1991, vastly more than the number killed in Zimbabwe. Officials blame robbers, but Mr Auret fears that a “sort of force” may be organising them.

A new pressure group, the Landless People's Movement, which claims 100,000 members, threatens farm invasions next year. Its leaders also say they will disrupt South Africa's pending general election, with the slogan “no land, no vote”, unless land is redistributed faster. Last weekend, the agriculture minister, Thoko Didiza, met them.

South Africa is not Zimbabwe, however. South African squatters usually demand space to build houses, not to grow crops. Granted, the government does say it wants 30% of agricultural land to be in black hands by 2015, to promote black commercial farming. But there are many farms for sale, and a price that suits both parties can usually be agreed.

Restoring land seized under apartheid has been painfully slow but is picking up speed: of the 65,000 claims lodged by 1998, 46,000 have been resolved. In many cases claimants take cash compensation, leaving a white farmer, perhaps with a 99-year lease, to plough on.

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Italian politics

Berlusconi rebuffed

Jan 15th 2004 | ROME
From The Economist print edition

A bad week in court for Italy's embattled prime minister

REX

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IN ITALIAN courtrooms, above the judges' bench, is displayed a ringing declaration: “The Law is Equal for All”. On January 13th, Italy's highest court decided that this means what it says. The constitutional court struck down a law passed by parliament last June granting immunity from trial to the state's five most senior officials, including the prime minister, Silvio Berlusconi. The issue had been referred to the court by judges in a case against Mr Berlusconi that was suspended when the law came into force last July.

Although the court has not yet given its reasons, it hinted that it agreed with both points made by judges in a lower court. The appellants had argued that the law violated two articles of the constitution: one that Italians are “equal before the law”, and another that guarantees them the right to defend their interests in court. By providing automatic immunity, the act stripped the five office-holders of their right to take on accusers before a judge.

For Italy's increasingly embattled prime minister, the constitutional court's decision was not so much a slap on the wrist as a punch in the mouth. It was the second time in a month that those charged with guaranteeing fair play in Italian public life had decided that his government was threatening it. Last month President Carlo Azeglio Ciampi refused to sign into law a bill that he believed would reinforce the overwhelming dominance of Mr Berlusconi's mighty media empire. Even some of the prime minister's supporters must be wondering whether all this is really only a plot against Mr Berlusconi, as he and his allies still insist.

“Damned communists”, was how one deputy of the prime minister's Forza Italia party greeted the court ruling. “It's a disgrace and a demonstration that the constitutional court is a political institution,” said Carlo Taormina, who—like several other Forza Italia lawmakers—is a member of Mr Berlusconi's personal legal team. It was reported that the court had split 10-5. Government supporters say this reflects its political make-up. Most of its judges were appointed by Mr Ciampi's predecessor, Oscar Luigi Scalfaro, who clashed repeatedly with Mr Berlusconi when he was previously in office in 1994.

Yet that scarcely makes the judges “communists”. Mr Scalfaro is a lifelong Christian Democrat and devout Roman Catholic. Like Mr Ciampi, though, he felt that Mr Berlusconi needed restraining. The prime minister's supporters counter that the immunity they proposed is guaranteed to heads of state and government in some other democratic countries. That is a fair point. Yet, as so often with the Berlusconi

government, the suspicion remains that possibly defensible legislation was being proposed for indefensible motives.

The suspended trial, in which Mr Berlusconi is accused of bribing judges, will now have to be reopened within two months. And it may not, as originally expected, have to start again from scratch, which would ensure that the prime minister would benefit from a statute of limitations. A new panel of judges will be sworn in, but the man who will head it, Judge Franco Castellano, was quoted this week as saying that most of the evidence already admitted was “fully valid and usable”.

Last November, Mr Berlusconi's former lawyer, Cesare Previti, was cleared of one of the charges levelled at Mr Berlusconi. But he was convicted of a related corruption charge. A restarted trial is thus likely to occupy Mr Berlusconi's time with legal concerns and get in the way of the centre-right's declared intention of reforming and modernising the country. None of this will restore unity to the fragile coalition: several parties are unhappy, and the Northern League is threatening to quit. It is not impossible that Mr Berlusconi may try to cut through his troubles, and wrong-foot the opposition, by calling fresh elections in the next few months.

Antonio di Pietro, the anti-corruption prosecutor-turned-politician, said that the constitutional court's ruling would restore faith in Italy as a country governed by the rule of law. But more court cases involving Mr Berlusconi will also draw attention to claims of low ethical standards in Italian business and public life. With the inquiry into the bankruptcy of the food group Parmalat now pointing not only to fraud on a huge scale but also to the involvement of politicians as well as businessmen, Italy's image has seldom been worse.

Mr Berlusconi's troubles do not end there. In another court case this week, a Rome judge dismissed his libel suit against *La Repubblica*, which had reprinted much of an article about Mr Berlusconi's past that appeared in *The Economist* in April 2001. The judge said she had no jurisdiction over the libel suit against *The Economist*; if Mr Berlusconi wishes to proceed, he will have to start again in Milan. She also ordered him to make a contribution to both defendants' costs.

Amid all the judicial clamour, the most ominous sound may have been the total silence of the prime minister himself. The biggest danger of all is that a wounded, cornered Mr Berlusconi could initiate a conflict between the executive and judiciary more ruthless than anything seen so far. “The [immunity law] allowed a truce,” his justice minister, Roberto Castelli, said. “The verdict of the constitutional court could again unleash the war.”

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Migration in the European Union

The coming hordes

Jan 15th 2004
From The Economist print edition

Fears of migration from east to west

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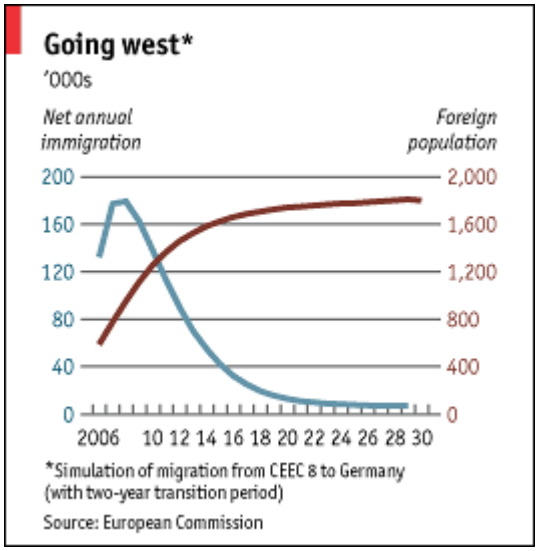

ON ONE side stand economists armed with formulae and tables of data, arguing that migration from the poor countries of central Europe to the rich countries of western Europe will be modest and manageable after ten new members join the European Union in May. On the other stand Eurosceptics, trade unions and some governments, worried that enlargement will bring a rush of migrants chasing jobs and social-security benefits. Almost drowned out are voices from the poor countries themselves, demanding the rights and freedoms of EU membership, but fearing a drain of skilled workers.

Free movement of workers across borders is a basic EU policy. But it poses problems of scale when the EU is gaining ten countries, with a combined population of 75m, that have wage levels and living standards far below the 15 existing member countries (and 380m people). Cyprus and Malta apart, the new members include eight central European countries with an average income per head of only 23% of the EU average in 2001. That figure falls to 18% if Bulgaria and Romania, which hope to join in 2007, are added.

Given such a big income gap, and high unemployment in many of the new countries, the question should perhaps not be why so many workers might want to leave, but why so many might choose to stay. One answer is that prices are lower in central Europe, making those low average incomes worth more like 35-45% of their west European counterparts. But that still leaves plenty of incentive for workers to go overseas, send money home, and come back to spend it later. Already more than 400,000 migrants from central Europe are working legally in the EU, and many others are doing so illegally.

Fears of a big new migration wave from central Europe after enlargement have provoked a policy split among EU governments, already hard-pressed by asylum seekers and illegal immigrants from farther afield. Germany and Austria, which border the new members, oppose a quick opening-up of labour markets. They have secured agreement that EU members can restrict labour inflows from central Europe for up to seven years, although this should not affect students or tourists.

Britain and Ireland are among the countries taking a quite different view. They have promised to open their labour markets immediately, seeing workers from the new countries as a timely source of cheap, skilled labour. Some EU governments have yet to state final positions, though the European Commission hopes they will do so by the end of January. They all have the option to bar workers from central Europe for an initial two years, and to renew this bar for another three years in 2006. A further extension of two years will be possible for countries that still fear “serious disturbances” in labour markets.

Recent academic simulations have predicted that as many as 3m-4m people will migrate from central to western Europe in the 25 years after enlargement, about 1% of the present EU population. Roughly half of those will be workers. There will be a first surge of migrants for two or three years, then a falling away (see chart). Based on past trends, at least half the migrants will head for Germany.

Those who think the rate of migration will be higher point to German unification, when over 7% of the population moved from east to west in ten years, despite a huge flow of subsidies from west to east.

Those who think it will be lower cite the EU's experience with Spain and Portugal, which joined in 1986. There was no big outflow then: rather the opposite, as strong growth at home attracted Spaniards and Portuguese back from other countries. But when they joined, Spain and Portugal had living standards much closer to the EU average than the countries of central Europe do now. Spanish purchasing power was about two-thirds of the EU average. For Poland, the biggest country in central Europe, the figure is about 40%.

Even diligent and legal migrant workers from central Europe could pose political problems for western European governments, if they come in large enough numbers and seem to price locals out of jobs. But they will still be valuable economically, because they are likely to contribute more in work than they take out in pay.

The bigger worry for rich-country governments concerns migrants in search of state benefits. Central Europe's Roma minorities—about 9% of the population in Slovakia, 5% in Hungary and 3% in the Czech Republic—are a particular cause for concern. The poorest Roma villages, especially in eastern Slovakia, are among the most desperate places in Europe, with no work and little schooling. A flow of Roma migrants claiming political asylum led Britain to reintroduce temporary visas for Slovaks a few years ago. Such barriers will be illegal after EU enlargement.

Yet whatever problems migration may pose, short-term restrictions, such as those proposed by Germany and Austria, will not be a solution. At best they may merely delay or divert flows. A two-year or even five-year delay is not much when set against the 50-90 years that it might take the countries of central Europe to catch up with west European living standards. If the incentive to migrate from central Europe is strong in 2004, it will be strong in 2009—unless western Europe's economies do remarkably badly.

A better way to deter too much movement of people would be through investment in the poorest parts of central Europe, especially improving infrastructure such as roads. This should bring businesses and jobs, making it less likely that people will migrate. That is a good argument for directing eastwards the subsidies that the EU gives to poor regions.

Even so, east-west migration will be a fact of life in the EU for at least the next 30 years. The trick is to make the best use of it. This means fine-tuning benefit systems to shut out short-stay claimants, as Denmark is doing, and improving incentives to work. It means deregulating labour markets so that jobs can be created cheaply but legally for the workers who want them. Migration will be less of a challenge, and more of an opportunity, if it forces such reforms on recalcitrant governments.

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Jobs in Europe

The lure of Brussels

Jan 15th 2004
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Runners and riders for top European jobs

SOME of the best-off migrants going west this year will be taking jobs in European institutions. Many will earn far more than heads of state at home: one study from Speyer University says that, on average, Euro-MPs from the ten new countries will get three times as much as their prime ministers. But the biggest cheeses will be the ten European Commissioners arriving in May. Romano Prodi, the commission president, wants candidates by end-February.

The signs are that the acceding countries will play it dismayingly safe. There will be no larger-than-life characters like the Czech Republic's Vaclav Havel or Poland's Lech Walesa to disrupt the mix. The nominees will be mostly former foreign ministers, Europe ministers or chief negotiators in the accession talks.

At least three of the ten are likely to be women—slightly correcting the sex balance of today's commission, which has five women among its 20 members. Latvia wants to send its foreign minister, Sandra Kalniete; Lithuania is proposing its finance minister, Dalia Grybauskaite, a former diplomat with a black belt in karate; and Poland is likely to nominate its Europe minister, Danuta Hubner.

Other candidates include Siim Kallas, a former prime minister of Estonia; Milos Kuzvart, a former Czech environment minister; and Janez Potocnik, Slovenia's Europe minister. Hungary is leaning towards Endre Juhasz, a deputy foreign minister. Only in Slovakia has the choice become openly acrimonious: the prime minister, Mikulas Dzurinda, wants to send a businessman, Ivan Stefanec, but others in the coalition favour Jan Figel, who led the accession negotiations.

The newcomers will have little to do, as Mr Prodi's commission will have only six months of its term left. They have more hope of making a mark in the new commission that takes office in November. But it is open to question, even then, how many will have jobs worthy of the name (and pay). The commission is already overmanned with 20 members, one from each small country and two from each big one. In May, it will balloon to 30, before a new commission of one per country takes over. But that will still mean 25 top people jostling for duties that could be shared better by 12.

Commissioners from newer and smaller countries, lacking in experience and clout, are likely to end up with the junior jobs. But better that than nothing, say their governments. In the debate on a new EU constitution, these countries argued most forcefully against trimming the commission to a niftier size. They see guaranteed representation in Brussels as the best safeguard against an EU run by (and for) its biggest members.

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German defence

Reforming reticence

Jan 15th 2004 | BERLIN
From The Economist print edition

Germany is trying to adapt the Bundeswehr to the post-cold war era

"WHAT if there were a war and nobody showed up?" German pacifists once asked. In future, Germany's armed forces will at least be able to show up, if their political masters so decide. On January 13th, Peter Struck, the defence minister, announced a reform of the *Bundeswehr* that should make it easier to send troops to far-flung places.

Not before time. Over the past decade, political and legal roadblocks to German military action in trouble-spots have gone, but practical problems remain. Unlike Britain and France, Germany has been slow to adapt to a world in which conventional war in defence of the homeland is unlikely. Despite having 285,000 soldiers and an annual budget of over €24 billion ($30 billion), the *Bundeswehr* has had trouble mustering and equipping the 7,000-odd Germans on peacekeeping duty in Afghanistan and elsewhere.

Why is the *Bundeswehr* such a lumbering dinosaur? In the cold war, it was a huge army dominated by conscripts whose notional job was to stop the Red Army. Such forces are not much use for the likely jobs of the future. Yet preparing for real, not imaginary, tasks is likely to require a spike in defence spending, and Germany is heading the other way.

Mr Struck's reforms at least take on the challenge. He proposes to shrink the number of soldiers to 250,000, in order to boost, from 25% to 30%, the share of the military budget that goes on new weapons. He is also making big structural changes. In a move that American defence planners might envy, the army, air force and navy will be linked into a single force geared to rapid, long-range deployment. The core of the new *Bundeswehr* will be a 35,000-strong "intervention force" for fighting and a 70,000-strong "stabilisation force" for peacekeeping, with "support forces" of 137,500.

Procurement plans have been revised, freeing an extra €26 billion over 15 years. Heavy weaponry to defend German territory is out, equipment to support rapid deployment is in. At the top of Mr Struck's wish-list are a joint forces information system, reconnaissance equipment and armoured transport vehicles. But, to his frustration, long-running projects like the Eurofighter still gobble up funds.

Can Mr Struck prepare the army for the future while meeting his obligations to NATO, the EU or the UN? Germany will fulfil its commitments, the minister insists. But the reform plans imply that Berlin has no intention of raising defence spending from a feeble 1.5% of GDP, one of the lowest among big rich countries (see chart).

Inside Germany, the main issue remains conscription and the *Zivildienst,* the civilian alternative to military service. Although Mr Struck denies it, some analysts see his plans as the beginning of the end for the draft. The conscripts, whose number will be cut to 50,000, could be replaced by professional soldiers. But if the draft went, so would its alternative, and that would cause problems for many social services that rely on conscientious objectors.

The other reforms have so far caused little uproar. But this may change. In the past, the *Bundeswehr* has mostly done easyish jobs, even in distant places. But the logic of Mr Struck's plan is that German soldiers will, one day, do real fighting. Only then will it be clear that the country has overcome its "culture of reticence".

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Turkey and Cyprus

Erdogan's gamble

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From The Economist print edition

A shift on northern Cyprus may help Turkey's European ambitions

THIS year has started auspiciously for Tayyip Erdogan, Turkey's prime minister. That is just as well, because he has many hurdles to leap before December, when the European Union will either honour or withdraw its conditional promise to open membership talks.

The stakes could hardly be higher. As the Turkish leader, who preaches a mild version of Islamism, argued in Berlin recently, a slap in the face from Brussels would convince not only Turks, but Muslims everywhere, that the EU had decided to be a Christian club. That may be an exaggeration. But if Turkey fails to win its invitation to formal talks, democratic and economic reforms may be derailed; and Islamic militancy could grow.

For anybody who wants to avoid that, every tactical victory chalked up by Mr Erdogan is good news. He seems to have scored one this week by laying the ground for a shift in Turkish policy on Cyprus. Negotiations on the future of Cyprus, which is to join the EU in May, will have a big effect on Turkey's own European prospects—as Romano Prodi, who this week became the first European Commission president to visit Ankara since 1963, will have reminded his hosts.

At the very least, talks between the island's Greek and Turkish sides over a UN-sponsored peace plan—the failure of which is widely blamed on Rauf Denktash, the Turkish-Cypriot leader—must restart. There is some urgency, because the Greek-Cypriot government will be admitted to the EU in May with or without a settlement. In the short term, the island's internal division might then harden.

The chances of progress on Cyprus have now improved—thanks to political developments on the island that Mr Erdogan helped to engineer. Mehmet Ali Talat, a left-leaning Turkish Cypriot who favours the reunification of the island under the UN plan, has formed a government in coalition with Serdar Denktash, a more obdurate figure in the mould of his father, Rauf. The word in Ankara is that Mr Erdogan all but ordered moderates and hard-liners to share power. He got his way in the face of opposition from military hawks, led by General Aytac Yalman, say aides to Mr Erdogan. Some claim this is a sign that Turkey's top brass are being tamed.

The next crucial step is to get the UN secretary-general, Kofi Annan, to sponsor a new round of reunification talks. Exasperated by the energy he has already wasted, Mr Annan has said he will restart the process only if both sides agree to hold referendums on the settlement before May 1st. If those ballots produce a “yes” vote, the UN would sort out the remaining details. The UN, in other words, has had enough of Cypriot manoeuvring.

If the Turkish side now agrees to a version of the Annan proposals, the onus will then fall on the Greek Cypriots, who are far from enthusiastic about the plan. Tasos Papadopoulos, the Greek-Cypriot president, has already said that he is against a referendum before the conclusion of negotiations. But if the plan ultimately founders on Greek rather than Turkish intransigence, Mr Erdogan will at least have boosted his European credentials and taken a step closer to Brussels.

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France and Muslim countries

Veil of tears

Jan 15th 2004 | PARIS
From The Economist print edition

The French government courts unpopularity with Muslim countries

Get article background

AFP

Tricoloured in Beirut

A YEAR ago, in the depths of his falling-out with America over Iraq, France's President Jacques Chirac could console himself with the thought that in Cairo and Rabat, at least, he was a hero. France's staunch opposition to the war won him a level of adulation that is rare for a western leader. Last October, in a Gallup poll in Iraq, Mr Chirac's popularity ranking (42%) dwarfed that of President George Bush (29%). Yet today, after his proposal to ban the Muslim headscarf in French schools and public offices, it has turned sour.

Since Mr Chirac proposed the law in mid-December, indignation in the Muslim world has been fierce. Veiled women have demonstrated against France in Cairo, Tehran, Gaza and Amman. Last week, 5,000 protested in Beirut. “The French authorities will not succeed in banning the Islamic veil in schools,” declared Ali Akbar Rafsanjani, a former Iranian president. “But if they succeed, millions of Muslims will curse them.” Islamist groups have called a day of protest on January 17th.

Officially, France insists that its cordial relations with the Muslim world are unaffected. (Last week, for example, France and Libya agreed on compensation for those killed in the 1989 bombing of a French aircraft.) Besides, many protests have been organised by extremist Islamic groups. There have been no official protests from governments in the Muslim world.

Unofficially, however, the French are worried. Mr Chirac's speech proposing the ban was rapidly translated into Arabic and English. French ambassadors were told to go out and explain that this was not an attack on Islam, but a domestic French matter. Nicolas Sarkozy, the hyper-active interior minister, jetted off to Cairo; he secured a declaration from Mohammed Sayyed Tantawi, a prominent Sunni religious authority who leads the al-Azhar mosque, that women in non-Muslim states should obey local laws, and—by implication—that not covering their heads was acceptable.

This week, Dominique de Villepin, the foreign minister, dropped in on five Gulf states to counter the belief that France was proposing an outright ban on the veil. The law to prohibit “obvious” signs of religious affiliation merely reinforces France's secular tradition, he insisted. “It is false to say that it is aimed at Islam and the wearing of the veil in particular.” The trouble is that many Muslims still see it this way, both within and beyond France.

Although most French people (69%) back a ban, the issue divides French Muslims. A survey of Muslim women in *Elle* magazine had 49% in favour and 43% against. The dispute is tearing apart the French Council of the Muslim Faith, set up by the government last year to provide a voice for Islam. Its president, Dalil Boubakeur, has discouraged Muslims from joining the marches on January 17th. But other Islamic groups, which dominate the council's regional board, call the protest “legitimate”. This week's appointment of a Muslim prefect in Jura will not calm fears that Islam is being stigmatised.

The government is determined to press ahead with the ban for the new school year in September. It wants to put right misunderstandings about the French secular state and the obligations of religious groups. Its position is certainly clear—but so might be the damage to relations with Muslims at home and abroad.

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Charlemagne

Government by judges?

Jan 15th 2004
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The European Court of Justice emerges blinking into the limelight

THOSE who believe that judges should deliberate in isolation from the hurly-burly of the real world would love the European Court of Justice. Situated on a windswept plateau in Luxembourg, the ECJ is so calm that you feel like apologising if you shut a door too loudly. But its quiet life may be about to end. The court's diet of competition and single-market cases has just been supplemented with the hottest of political potatoes. On January 13th the European Commission, the EU's civil service, said that it would sue the Council of Ministers, representing EU governments, for violating the euro area's "stability and growth pact".

In theory, the stability pact limits the budget deficits of the 12 euro-area members to 3% of GDP, on pain of possible fines. This year, France and Germany will have exceeded those limits for three years in a row. Yet when the commission proposed to force the two miscreants to make budget cuts last November, the Council of Ministers overruled it, deciding instead to put the pact "in abeyance". The commission argues that the council had no power to do this. The ECJ's ruling in this case, which may be its most important ever, could fundamentally affect the balance of power between the centre and the member countries.

Vassilios Skouris, a Greek professor who took over as president of the court last October, says that it is not new for the ECJ to be at the cutting-edge of defining the powers of the EU. He notes that "it is no secret that the case law of the court has been a major driving force towards European integration." Over the years court rulings have established such key principles as the supremacy of EU law over national law and the right of citizens to have European law enforced in their domestic courts. Just as decisions of the Supreme Court drove the expansion of federal power in the United States, so the ECJ has helped to establish a federal legal order in Europe. In both cases, an emphasis on removing barriers to trade helped to expand federal powers. And, as with the Supreme Court in its more expansive moods, ECJ decisions have often reflected a clear federalist ideology. Renaud Dehousse, author of a book on the court, concludes that "the ECJ has promoted a pro-integration line for decades."

One result of this orientation has been a steady expansion of EU powers, even into areas traditionally regarded as the preserves of the nation-state, such as tax, education and health care. Frits Bolkestein, the single-market commissioner, wrote recently that the ECJ is "increasingly taking over the role of lawmaker on crucial tax issues in Europe, not least in the area of company taxation." Gisela Stuart, a former British health minister who helped write the draft EU constitution, complains that "over the last decade a number of court judgments have step-by-step drawn health into the internal market."

New laws are likely to lead the court into fresh pastures. Fidelma Macken, the ECJ's Irish judge (each member country nominates one), predicts that the expansion of EU powers in justice and home affairs and the creation of a European arrest warrant will mean that "large numbers of lawyers specialising in criminal law will start appearing in our courts." If the EU ever agrees its new constitution, it is likely to include a Charter of Fundamental Rights, which will mean that the ECJ could be called on to define such things as "unjustified dismissal" or a "high level of consumer protection". The British government argues that the charter should not lead to a significant expansion in EU powers, because all the rights defined in the charter already exist elsewhere in EU or national law. But Judge Macken warns that it would be "foolish" to assume that the charter will have no impact on the court's jurisprudence. Indeed, some lawyers believe that, in time, the Charter of Fundamental Rights could become as influential as the American Bill of Rights in defining and developing federal power.

Luxembourg is no Washington

Judge Skouris acknowledges that the ECJ's role “has been comparable to that of the US Supreme Court.” But he points to two big differences: the ECJ cannot choose which cases to consider; and the appointment of judges is less politicised than in the case of the Supreme Court. “Candidates for the European Court are, to my knowledge, never scrutinised based on their views (ie liberal or conservative) that they have taken on specific legal issues,” he says. Individual voting records of Supreme Court justices are a matter of public controversy, but dissenting opinions within the ECJ are neither publicised nor explained.

These differences, plus the fact that the ECJ is based in sleepy Luxembourg, have meant that the court's role in defining and expanding EU powers has rarely attracted the same attention as Supreme Court rulings. But that period of political invisibility is drawing to a close. In recent years, the court has become a target of criticism for Eurosceptics. Paradoxically, its greater political visibility is coming at a time when it is becoming less reliably federalist. The notion that the ECJ is always in alliance with the commission has been undermined in recent years by a succession of negative judgments on commission decisions in merger and competition cases. That Belgium, France and Germany, the three countries said to be most in favour of “ever closer union”, also head the blacklist of countries that have failed to implement EU directives, and are therefore in danger of court action, further muddies the picture of a straightforward alliance between the court, the commission and ardent federalists.

The commission certainly cannot assume that it will get a satisfactory result on the stability pact. The law is complex, and even if the ECJ decides that the council exceeded its powers, it will struggle to enforce any judgment, still less to fine France or Germany. Ultimately the row over the pact will have to be settled politically, not judicially. At any rate, the judges know that this time they will be under the full glare of the media—something they may have to start getting used to.

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Social mobility

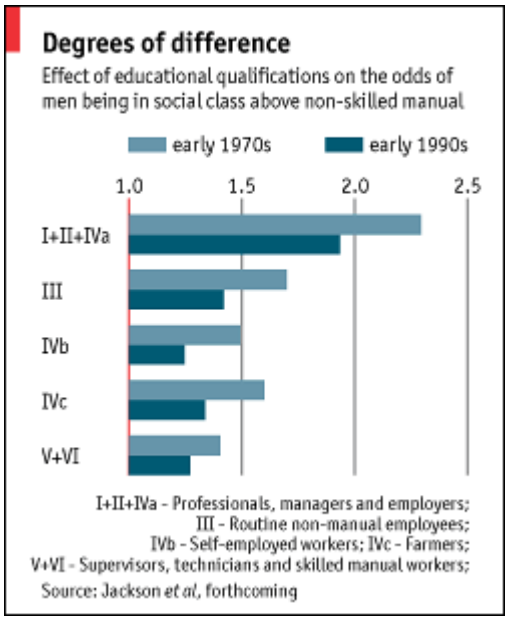
What's it worth?

Jan 15th 2004
From The Economist print edition

The government thinks more higher education means more social mobility. It's wrong

THE belief that more education will make Britain more meritocratic and shrivel the class system lies behind the huge expansion in higher education of the past two decades and the government's determination to steer half the country's 18-30-year-olds into universities. The idea that we live in a "knowledge economy" has strengthened that notion. But recent research casts doubt on it. Education plays a smaller role in social mobility than it used to, according to research which looked at the relationship of people's education to their careers in the early 1970s and early 1990s (see chart).

Why should the impact of education on social mobility be declining? Because, according to a forthcoming paper* by three academics at Nuffield College, Oxford, employers are becoming less interested in educational qualifications. That's happening for two reasons. Part of the job of higher education is to send a signal to employers—that someone has learnt to think, to persevere, to absorb information and to present ideas. As the supply of graduates grows, and the quality of teaching in Britain's shabby, crowded universities declines, this signal is fading. At the same time, services have been growing at the expense of manufacturing, and, increasingly, the qualities that employers in the service sector want are those the middle classes acquire at home: articulacy, confidence and smartness.



To test their hypothesis that employers pay little attention to educational qualifications, the Oxford researchers analysed 5,000 recruitment advertisements and interviewed people doing the hiring. Firms, they discovered, want recruits with skills that formal education does not necessarily bring: "high touch" in the jargon, rather than hi-tech. Typical examples are management jobs in fast-growing industries such as leisure and retailing, as well as posts in public relations, in sales and customer care.

Employers themselves say much the same thing. "What our members want is office and personal skills rather than more advanced education," says Matthew Knowles, policy adviser at the British Chambers of Commerce, a group for small and medium-sized businesses. "You see a lot of people from university who take three to six months to pick up the skills for an office job. They could do that by the age of 19 and start moving up. Instead they spend three years at college and then take a job they would have taken anyway."

Financial-services employers echo those views. Bruce Collins, chief executive of Tullett Liberty, a City broker, admits non-graduates to his graduate trainee scheme. "We want inter-personal skills, awareness, attitude, eagerness to learn: are they rounded individuals? What's their social life?" he says. "They've got to come across well, not just talk the numbers but build relationships." The result, he explains, is a workforce where a "guy with an O-level in woodwork sits next to a guy with a PhD in mathematics".

Marks & Spencer whittles down the 6,000 annual applicants for its 200 graduate trainee places entirely through tests of literacy, numeracy, reasoning and personality. This big retailer takes no account at all of the class or subject of degree, or the university attended.

All that chimes with the Oxford research, which showed formal qualifications featuring in only a quarter

of the advertisements in the sample, typically for top-level jobs. In the “sales and personal service” category, less than 10% stipulated educational qualifications. What these posts did require were skills in communication and team-working, and personal attributes such as “good appearance”, “good manners”, “character” and “presence”. Bad luck, then, for those who come across as tongue-tied, crass or nervous, regardless of their academic achievements.

Assuming, reasonably, that job adverts reflect what employers really want, this neatly explains why education matters less than the believers in meritocracy expected. “If you are selling high-value things like real estate, you will be interacting with middle-class people and you will do better if you are familiar with their style, manners etc,” says John Goldthorpe, one of the paper's authors. “It's not much use having some graceless anorak, however impressive his or her degree. The attributes that these people have from their family background have some real commercial use. It's not nepotism. Employers know what they want.”

Mike Hill, of Prospects, a state-funded career service, says “universities are encouraging people to develop just these skills—to speak in a businesslike way, to make small talk.” One example is Hull University, where a popular module in “career skills”, includes “the world of work”, time management and how to talk in a business environment. Great stuff—but not necessarily worth spending three years at university and running up many thousands of pounds in debt.

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*“Education, Employers and Class Mobility”, by Michelle Jackson, John Goldthorpe and Colin Mills, to be published in *Research in Social Stratification and Mobility* (Elsevier)

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Oxford University

A bargain

Jan 15th 2004
From The Economist print edition

The cost of an undergraduate

WHAT does it really cost to educate an undergraduate at Oxford University? Not £3,000 ($5,500) a year, the top fee the government will allow Oxford to charge if its education bill—and indeed, the prime minister—survives. A privately financed think-tank, the Oxford Centre for Higher Education Policy Studies (OXCHEPS), has commissioned the Ulanov Partnership, a consultancy, to take apart the university's finances. It has come up with an answer in an unpublished report: £18,600. That figure excludes accommodation and catering (not covered by the government's cap), and ranges from £17,100 for an arts degree to £20,900 for science. The number depends crucially on how core research costs are allocated: knock them out, and costs per undergraduate fall to £13,800. Either way, the current tuition fee of £1,125 pays less than 10% of the cost of educating a student.

The funding gap helps to explain why Oxford dons are paid one-third as much per teaching hour as their American counterparts. More important, they carry a much heavier teaching load than American dons. They have roughly twice as many undergraduates per don as Harvard or Princeton and less help with their teaching duties. At Harvard, there are half as many teaching assistants as dons; in Oxford, hardly any. Overall, Harvard appears to employ about five academic support staff (librarians, research technicians and so on) per don; Oxford employs just over two. Dons who flee Oxford for America often complain that what drove them was not the pay but the lack of help with mundane chores such as photocopying.

One implication is that Oxford is paying its way much more than is generally realised. OXCHEPS reckons that 58% of the costs of teaching come not from students or government but from private money such as conference earnings and endowment income. If the bill to raise fees fails, that will have to increase. Oxford is considering increasing the proportion of overseas students from 7% now to 12% in 2008, and the number of postgraduates (who pay more) from 5,400 now to 7,000.

The study has looked not just at Oxford's finances but also at its students' backgrounds. Oxford tends to be at the sharp end of Labour rhetoric because it is assumed to be full of grandees. But only 17% of Oxford students come from families with incomes of £60,000 a year or more; 42% from families with £40,000-50,000 a year.

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Employment

Return of the wrinklies

Jan 15th 2004
From The Economist print edition

Why the old are rushing back to work

BRITAIN'S labour market remains surprisingly robust. Unemployment continues to fall, reaching a record low of 4.9%; employment continues to rise. Most surprising of all, older people are grabbing the new jobs.

Over the past year, the number of people aged 50 and over who are working has risen by 190,000. Because of declines in other age groups, that exceeds the total increase in employment of 186,000. Much of the growth is among people older than the state pension age—60 for women, 65 for men—where employment rose by 73,000.

The trend towards early retirement has halted in Britain. Employment rates for people below the retirement age have risen markedly. For example, 71.5% of men aged 50-64 are now working, up from 65% in 1995. Since this age group has also been increasing in size as a result of the post-war baby boom, there has been a substantial increase in employment, from 4.8m in 1995 to 6.2m.

Until recently, however, few people carried on working beyond the retirement age. Over the past decade or so, the employment rate for this group has remained stuck at around 7.5%. But in the past couple of years the rate has jumped to 9.2% (see chart). Almost a million people now work beyond the traditional retirement age.

One reason is the tightening labour market. “Employers are facing skills shortages, so they are looking to retain older workers,” says Sam Mercer, director of the Employers Forum on Age, which campaigns against age discrimination.

Some companies such as the Nationwide Building Society have deliberately sought older workers for good business reasons. “Many customers prefer dealing with more mature and experienced people, and older workers tend to be more loyal and committed,” explains Carol Hurst, Nationwide's head of personnel.

Retiring early is no longer a cushy number. Companies have withdrawn provisions in their final-salary schemes allowing people to leave early on favourable terms. Older people saving for their retirement through money-purchase plans have been hit by falling annuity rates, caused by rising life expectancy and declining investment returns.

The recent upsurge in people working beyond the retirement age is almost certainly linked to the bear market in equities from 2000 to 2003. “People simply can't afford to retire because of the fall in the value of their funds,” says Deborah Cooper of Mercer, a pension-consultancy firm.

The return of the older worker points the way to solving Britain's pension problems. The House of Lords committee on economic affairs—whose members are aged 50 to 95—advocated raising the state pension age in a report published on January 10th. The government should take its august advice.

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Fish farming

Salmon a-slumping

Jan 15th 2004 | LOCH SUNART, ARGYLLSHIRE
From The Economist print edition

Economics is giving salmon farming more trouble than science is

ROSIE MACLACHLAN earns £15,000 ($27,700) as assistant manager of a salmon farm on Loch Sunart, at the foot of the Ardnamurchan hills. She's grateful. “Apart from work on the estate and seasonal hotel jobs, there's nothing much else here,” she says. But her job offers more beauty than security. The future of salmon farming in the Scottish Highlands and Islands, which employs 1,500 people, looks precarious.

Periodic health scares (see article) do not help, but the main problem is that supply has been growing faster than demand. Scottish farmed salmon production has swelled from 32,000 tonnes a year in 1990 to 145,000 tonnes in 2002. Output from Norwegian and Chilean fish farms has grown similarly, so wholesale prices have fallen from around £2.70 a kilo in 2000 ($1.90 a lb) to less than £2.20 a kilo now.

As a result, three small fish-farming companies in the Shetland Islands, where the cost of transporting feed and harvested fish is high, have gone bust in the past month. More collapses of small firms, caused by banks refusing loans to pay for buying young fish from freshwater hatcheries and transporting them to sea cages, look likely.

Even big firms are finding it tough. “Probably no one is making an acceptable return,” says Graeme Dear, managing director of Dutch-owned Marine Harvest (Scotland) Ltd, which produces about 30% of Scottish farmed salmon. Consequent cuts in production mean that prices and profits may recover this year, so long as people don't stop eating his fish. The signs from British supermarkets this week were that consumers had decided to ignore the latest health scare.

Mr Dear needs prices to recover to justify the cost of a new ship equipped with seawater tanks which transports live fish to processing factories nearer markets. “It adds 24-48 hours to the salmon's shelf life,” he says. This, he hopes, will give him a competitive advantage. But it will cost £1m a year. Smaller fish farmers cannot afford that. So the industry looks likely to consolidate as well as shrink. And although the mechanisation and computerisation of feeding has vastly increased productivity, cost pressures are also likely to force the fish farmers to group their cages together into bigger units.

That will draw the wrath of rod fishermen, who blame the spread of fish farming and the parasites that live on farmed fish for falling numbers of wild salmon in Scottish rivers. Conservationists, who complain that farms kill off sea-bed life beneath, are also likely to be upset. The farmers respond that this problem, which affects only small areas of the sea bed anyway, can be resolved by easing licensing restrictions to allow cages to be moved every few years. Environmental studies, they say, show that the sea bed returns to normal three years after cages have gone. But many rod fishermen and conservationists say the industry needs more, not less regulation—which would put up costs and reduce profitability still further.

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Poison in salmon

Fishy science

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How much salmon should you eat? It depends who you ask

ACCORDING to a paper published in *Science* on January 9th, levels of organochlorines in farmed salmon are so high in Scottish output that people should eat less than half a portion of salmon a month. Organochlorines are unpleasant chemicals such as dioxins and PCBs (polychlorinated biphenyls) produced by industry that hang around in the environment. Thanks to environmental regulations, there are far fewer of them than there were 20 years ago, but small amounts can still be found in all foods. They accumulate in animals, concentrating in the fatty parts. The authors of the *Science* paper looked at 700 salmon from around the world. Europe's salmon came off worst overall; among European salmon, Scottish fish did particularly badly.

Yet America's Food and Drug Administration (FDA) and Britain's Food Standards Agency (FSA) think there is nothing to worry about, so long as people eat the amounts they recommend. Contaminant levels reported in the study are easily within guidelines set by the FDA, the World Health Organisation and the European Commission. Because oily fish such as salmon helps prevent heart disease, the FSA thinks people should eat at least a portion a week.

So why did the authors of the *Science* paper come to such a different conclusion? Because they based their findings on the method of assessing toxicological risk used by a different regulator, the Environmental Protection Agency(EPA), to advise sport fishermen how much of the fish they catch they can eat.

The EPA method adds the different organochlorines together. The FDA looks at levels of individual chemicals. Some toxicologists say that the EPA method is appropriate only when there is certainty that chemicals have the same effect on the body. That is so in this case, says Jeffery Foran, one of the authors of the paper, president of an advocacy group, Citizens for a Better Environment, and a professor of natural resources and the environment at the University of Michigan: all four organochlorines studied cause liver cancer through the same mechanism. The FDA disputes this.

Wild European salmon (which the scientists did not check) may not be any less contaminated than farmed ones. Salmon get contaminated through their food. They are fed meal made from smaller fish, which are caught in the mucky waters of the North Atlantic. Kjell Bjordal, the chief executive of one of the largest fish-feed suppliers in the business, points out that wild European salmon feed in the same places as fish-food manufacturers gather their ingredients. On the positive side, though, Mr Bjordal adds that should regulators decide that organochlorine levels in fish feed are a problem, the industry has the technology to reduce them.

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Emissions controls

Breathe again

Jan 15th 2004
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Industry is unduly upset at tough new limits on emissions

CAN business live with Tony Blair's zeal to cut down greenhouse gases? All but very small companies already pay a “climate change levy” on their use of energy. Now Whitehall is about to issue stern new limits for some industrial emissions, notably by power generators. Since a third of Britain's electricity still comes from coal-fired stations, its price will be pushed up. How shall we compete, ask business leaders? A fair question, but the answer is: pretty well, and some of you will gain.

The main greenhouse gas, by far, is carbon dioxide, CO2. Britain put about 540m tonnes of it into the sky last year. On the basis of current policies, that would slide to 495m or so by 2020, but then rise again. Instead the government hopes to cut emissions to 240m tonnes by 2050. Hence the new limits.

At Kyoto in 1997 the EU agreed to cut emissions by 8% from 1990 levels by 2008-12. In 2002, EU countries settled how to share out this obligation: poor ones could pollute more than in 1990, some rich ones must cut harder, 12.5% in Britain's case. But now the government is going further still, setting limits for 2005-07 which, with tighter ones later, will bring Britain's cut to 20% by 2008-12.

They will be set, plant by plant, across the main energy-using sectors: Britain's share of a similar EU-wide scheme, covering 18,000 plants, which from early 2005 will impose fines of €40 (£28 or $50 today) at first, €100 later, per tonne of CO2 by which a plant exceeds its limit. Although Whitehall will now consult, briefly, before setting the details in stone, British business is “deeply concerned” at these “tighter limits, sooner”, says the CBI.

It fears two sets of price rises: electricity first, other inputs later. The wholesale price of electricity is expected to rise by 10-20%. Energy is typically 5% of the cost of basic industrial processes, though more for some. Builders watch out: electricity makes up 8% of the cost of making glass, 15% of cement and 20%-plus of bricks. Apart from energy, the sectors that will suffer include paper, oil-refining, cement, steel and foundries. These supply many others, and will try to pass on their costs.

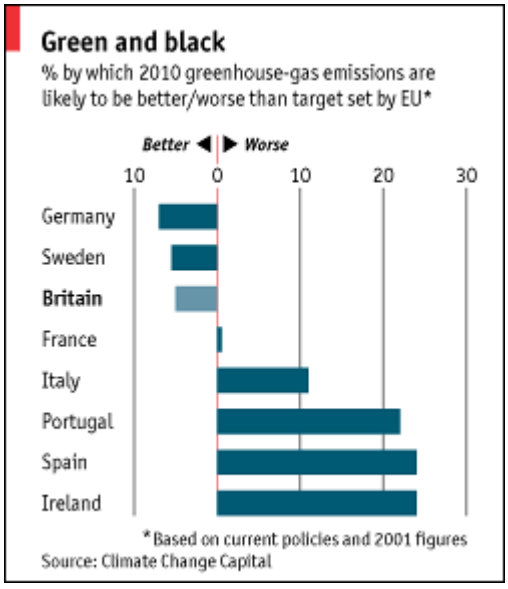
American firms face no Kyoto restraints, and British firms suspect that other EU members will not be as strict as Britain. Ireland, Spain and Portugal may not meet their 2002 EU targets, even though these meant increases, not cuts, in emissions, to allow for growth since 1990. And countries with stricter rules may not police them as firmly as Britain.

Another argument for less haste is the new EU emissions-trading scheme. It will let dirty plants avoid fines by buying emission allowances from clean ones. A sound, market-based idea: Britain already has a similar scheme, to let firms cut their climate levy. But the market has proved illiquid. Prices swing wildly. The EU version may work no better.

This all sounds like bad news for business. But figures from Climate Change Capital, a specialist finance house, suggest that the new limits may not do much harm. Britain is already far down the road, and with little extra effort could meet Mr Blair's targets. Power firms have long been switching from coal to cleaner and (normally) cheaper gas. They, and makers of other inputs that tend not to be imported (cement and packaging paper, for instance, though not newsprint), can usually pass on costs. But steel will suffer: its costs will rise more than most, and the trade is truly international.

And what of the firms to whom higher costs will be passed? The cost increases, though nasty, may spur them into speedier innovation. Cutting energy use or emissions need not be expensive, nor radical. While well-publicised wind power still needs heavy subsidy, advances in the now standard gas-turbine technology do not, and may save more. Ditto on the users' side. Simple changes, such as better insulated buildings, may be the most worthwhile. The biggest, though little-noticed, gains will come from step-by-step innovations in industrial processes.

Oddly, the seemingly sure winners are doing only fairly well. Energy or climate consultants? “Flourishing, not booming,” says one. Emissions auditors? After nearly two years of Britain's trading scheme, fewer than ten firms, led by the big auditors/consultants, are accredited.



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Prison suicides

Life and death

Jan 15th 2004
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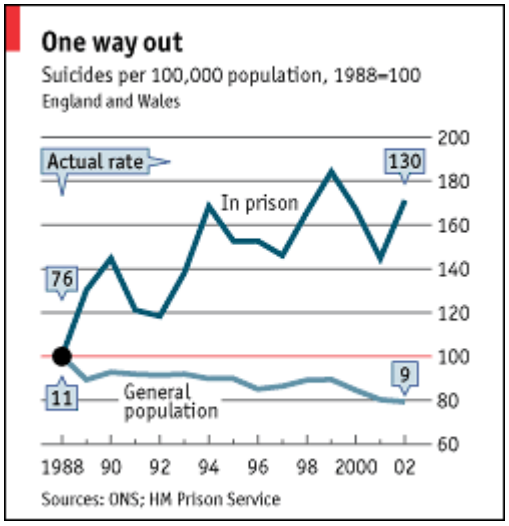
Harold Shipman's suicide was predictable, but not necessarily preventable



BELIEF in fire and brimstone is at such a low ebb these days that the suicide of a convicted murderer—even one as unpopular as Harold Shipman—looks less like a case of justice brought forward and more like evasiveness. Disappointment and anger followed the death of the Manchester doctor, who is thought to have killed at least 215 patients between the late 1970s and the late 1990s. Two inquiries have been launched, to discover how a man said to have acted “utterly normally” in prison could suddenly end his sentence after just four years.

Investigators may or may not find evidence of missed warning signs. Whatever they decide, Dr Shipman's death is ultimately as unsurprising as his behaviour towards the end of his life. British prisons are suicidal places: despite strenuous efforts to keep the toll down, and a general decline in suicide among the population at large, rates have drifted upwards over the past 15 years. Every year, more than one in a thousand prisoners take their own life, usually by wrapping a sheet around their neck, as the doctor did.

Much outrage has focused on the deaths of prisoners who have not yet been sentenced, and rightly so. Young, fearful, and often suffering from drug withdrawal, these new arrivals kill themselves in appallingly large numbers. But that is not so surprising, given that so many pass through the system. The chance that a given remand prisoner will end his or her life in prison is not unusually high. It is for lifers. At 8% of the prison population, and less than 1% of receptions, they account for 21% of suicides. Murderers and men who expect to die in jail are particularly likely to perish at their own hand.

While long-term prisoners are unusually likely to commit suicide, it is also unusually difficult to stop them. Alison Liebling, a Cambridge University penologist, says that lifers are unlikely to display warning signs before killing themselves, or to have a history of self-mutilation. They are also prepared to wait for a good opportunity. “For lifers, suicide is a rational choice,” she says. “They simply decide it isn't a life they want to live.”

There are ways of reducing deaths among long-term prisoners, but unfortunately, they tend to mean eroding the few privileges that make their lives bearable. Inmates can be checked every 15 minutes, as Dr Shipman was at the beginning of his sentence, but that means denying them privacy. They can also be made to share cells—a practice that has held down suicide rates in American prisons—but that can induce despair.

The death toll is likely to worsen over the next few years. For one thing, there are many more lifers: 533 were received into the system in 2002, up from 236 a decade earlier. And they have less and less reason to hope for an early release. Dr Shipman, like many other long-term prisoners, kept abreast of the news (he read the *Guardian*). He may have noticed, last week, the introduction of new minimum sentences for mass murderers. Announcing the change, the Home Office declared that, for more prisoners than ever before, life would henceforth mean life.

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Traffic wardens

Unlovely Rita

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Deregulation has made traffic wardens more effective. Hooray

ASK a Londoner—particularly a middle-class Londoner—how to raise standards of law and order in their city, and they are likely to talk about putting more officers on the streets, upping the number of minorities in uniform, and cracking down harder on minor quality-of-life offences. Which is odd, because parking attendants, who excel in all three respects, are almost universally detested.

Parking attendants came into existence a decade ago, when traffic wardens (yellow and black-hatted adjuncts of the police) were stripped of their monopoly over petty parking offences. The new breed, who wear uniforms of various hues, are employed by local councils either directly or via private contractors. Over the years, their reach has grown: having pushed the old “wasps” off meter duty, they were eventually handed control of parking at public events, and, last week, over drivers who do naughty things like nip into bus lanes and block box junctions.

As an experiment in deregulation, these reforms have, so far, been strikingly successful. Numbers of ticket-writers have more than doubled, from around 800 in early 1990s London to 1,800 today. As the capital's drivers will attest, they are extremely productive, handing out almost 5m fines in 2002.

The new enforcers look different, too. Forty-five percent of those employed by APCOA, a parking contractor, are black Africans, with most coming from former British colonies. Almost uniquely, these immigrants combine numerical competence and fluent English with a willingness to work for £6.50-7.00 an hour. As one Liberian parking attendant (who, like many of his fellows, holds a university degree) puts it: “There's a lot of stigma attached to the job. The average white boy would rather be on the dole.”

Like other effective foreigners, parking attendants have met with scant approval. Even cool-headed Londoners complain that the new breed is less sympathetic to drivers' entreaties than old-style traffic wardens. To an extent, this is true: attendants enjoy much less latitude in deciding whether to write a ticket. The introduction of a harder line was intended to protect them, on the grounds that reducing arguments would reduce violence. But it hasn't worked out like that. Nick Lester, transport director for the Association of London Government, says that assaults on parking attendants have risen steadily since deregulation.

For many years, the attendants were especially disliked by the police—who, even more than other citizens, tend to think they are above parking regulations. Coppers talked of them as though they were an enemy army: Mr Lester relates one story about traffic wardens going into a police canteen, only to be met with Nazi salutes.

These days, though, the police are exploring the possibility of symbiosis. Recognising that parking attendants do some of the things that, nostalgia suggests, coppers ought to do (walk a regular beat; engage with the public) they are trying to woo them with promises of improved protection. Parking attendants now walk out with police officers; in time, they may be given police radios. And so the outcast is welcomed back into the fold.

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Bagehot

Blair-baiting

Jan 15th 2004
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It's not tuition fees they don't like, it's Tony

Get article background

IT IS becoming clearer by the day that the threatened rebellion over university tuition fees, when the vote takes place on January 27th, will have less to do with the future of higher education than with the desire to wound Tony Blair, preferably mortally.

No doubt, a good many of the 160 Labour MPs who signed a House of Commons motion back in November attacking variable fees had genuine concerns about the effect of the proposed legislation on university access. Quite a few were hostile in a knee-jerk sort of way simply because they had not taken the trouble to understand exactly what the government was trying to do and why it was important. Others were hoping to force financial concessions to allay their anxiety that poorer students might be deterred from going to university by the prospect of taking on large debts. Although manifestos are hardly sacred texts, a handful of the rebels may even have been genuinely offended by what they (legitimately) saw as a breach of the promise in 2001 not to bring in top-up fees.

If there was once an excuse for ignorance, that has all but disappeared. The education secretary, Charles Clarke, and the higher education minister, Alan Johnson, have been holding non-stop seminars explaining both the logic and the justice of their policy. Mr Clarke is persuasive in the way that tanks are, while Mr Johnson, a former postman and trade union leader who missed out on a university education, is not only charming, but usefully immune to the charge of elitism.

With the revised package of more generous bursaries for students from poor homes and easier loan repayment terms announced by Mr Clarke last week, the most fervent egalitarian now has little to complain about, as some are prepared to acknowledge. Even the fear that the £3,000 ($5,500) annual cap on fees may be very temporary has been partly assuaged by the government's undertaking that any change will require parliamentary approval.

All of this has helped. So too has the response of the rebel leaders, who have provoked a minor backlash by setting up their own rather crude whipping operation to stiffen the resolve of waverers. A conveniently leaked memo from George Mudie to Barbara Roche, both former government whips, mentioned by name MPs who were having second thoughts and would have to be “dealt with”. The embarrassing implication, previously denied, is that they are operating as an organised caucus within the party, conspiring to defeat the government in a manner akin to the Maastricht rebels who harried the Conservative government of John Major to its eventual destruction.

Quite where this leaves the parliamentary arithmetic is uncertain. There are indications that the government is at last beginning to make progress. Attending a highly-charged meeting of Labour MPs on Wednesday, Mr Clarke had a better reception than expected, with only one out of about 30 speakers overtly hostile. There is also now a steady dribble of MPs explaining why they may be ready to switch sides. Some suggest the government has done enough to be given the benefit of the doubt, while others resent the rebel ringleaders' tactics.

Critically, there is a growing realisation that this is not really about university funding, but about Mr Blair's leadership. At least a few have enough sense to recoil at being caught up in a plot to get rid of the most electorally successful leader in Labour's history. Government whips are confident that between 50 and 60 signatories of the anti-fees motion will now either vote with the government or abstain. That leaves about 100 still intent on mischief and the government at least 20 votes short of what it needs to guarantee victory by the smallest margin.

Gordon's call

What can be said about the remaining rebels? They are an over-lapping coalition of embittered ex-ministers, the traditional left (both hard and soft) who have never much cared for the prime minister, and supporters of Gordon Brown who are eager to hasten the day when the chancellor receives what is rightfully his. Most of them voted against the government over Iraq and claim not to have forgiven Mr Blair for his “deception”.

Clare Short, a former cabinet minister who resigned last year, is blunter than most, but her views are typical. This week she said of Mr Blair: “The possibility he might have to go and be replaced is no longer a frightening prospect. The Labour Party is crumbling away to disillusionment and a tremendous loss of members—a new spirit would renew the party and the country.” Ms Short, unsurprisingly, believes that, if Mr Blair loses the vote on tuition fees, he will have to go.

Mr Brown appears to be loyally doing his best to persuade his allies—who include Ms Short, Mr Mudie, Ms Roche and the former chief whip, Nick Brown—to pull back. But because of his supposed previous lack of enthusiasm for top-up fees and his disdain for Number 10 advisers, who are the principal architects of the policy, until this week he had not been heard quite loudly and clearly enough.

Yet, paradoxically, it is as important for Mr Brown that this unprincipled revolt be seen off as it is for Mr Blair. The prime minister's political survival may not be the chancellor's overwhelming priority. It is, however, very much in his interests, both now and in the future, for Labour to be capable of governing. A victory for the rebels would not necessarily spell the end for Mr Blair, but it would be a powerful signal that Labour, like the Tories after the removal of Margaret Thatcher, had ceased to be a party worth leading.

However much Mr Brown wants to be prime minister, he knows that there could be few worse ways for him to achieve his ambition. Which is not a bad reason for thinking that somehow the government will get its legislation through.

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First get the basics right

Jan 15th 2004
From The Economist print edition

AP

Africa remains poor mainly because of bad government, says Robert Guest (interviewed here). The remedies look simple, but will be hard to apply

THE view from the pick-up truck rolling through the Zimbabwean countryside was grim. Field after field that should have been prepared for planting was idle and choked with weeds. But the farmer driving the truck—let's call him “Dave”—had no time to stop and grieve. He had an appointment to get his tractors back.

As part of President Robert Mugabe's programme of “land reform”, Dave's big farm had been carved up among half a dozen members of the ruling party, ZANU-PF. These middle-ranking cronies had in turn been thrown off by a big shot, a former brigadier with his own militia, who grabbed the lot for himself.

Under Zimbabwean law at the time, black would-be farmers allocated plots of formerly white-owned land were supposed to take only the land. The crops, cows and combine harvesters were deemed still to belong to the people who had sown, reared or bought them. But when Dave tried to salvage his moveable possessions, the brigadier's bodyguards blocked his way. So Dave got himself a court order and a promise of an armed police escort to help him reclaim this modest fraction of his life's accumulated assets.

He arrived at the local police station at the appointed hour, with some friends to help and your correspondent, incognito, to observe. The armed escort did not show up. The police chief shrugged and mumbled excuses. Then the brigadier stormed into the police station to complain that someone (possibly the farmworkers he had evicted) was stealing “his” crops at night. The police immediately dispatched a car and four officers to assist him. It was a striking vignette of how selectively the law is applied in Zimbabwe. Property rights are secure only to the extent that you enjoy the favour of those in power.

Land reform was supposed to benefit the poor, and indeed some 134,000 people have been allocated plots. Mr Mugabe promised the new farmers seeds and fertiliser, but delivered almost none, partly because he has evicted the farmers who used to grow the seeds. Few of Zimbabwe's new farmers know much about farming, so yields have plunged. Half the population now depends on food aid, which the ruling party shamelessly tries to reserve for its own supporters. There is a harsh partisan logic to this. Didymus Mutasa, ZANU's foreign-affairs secretary, once said the country would be better off with only half its current population, “with our own people who support the liberation struggle”.

A continent in need of leadership

Sub-Saharan Africa (hereafter, “Africa”) is the world's poorest continent: half of its 700m people subsist on 65 US cents or less a day. Even more worryingly, it is the only continent to have grown poorer in the past 25 years, despite the explosion of technology and trade that has boosted incomes in other regions. Not even Africans want to invest in Africa: an estimated 40% of the continent's privately held wealth is stashed offshore. This survey will ask two questions. Why is Africa so poor? And what are Africans doing about it?

The short answer to the first question is “bad government”. As recent events in Zimbabwe show more vividly than any economics textbook could, rulers who respect neither property rights nor their own laws swiftly impoverish their people. No other African country has regressed as fast as Zimbabwe has over the past five years, but several have made similar mistakes in the past from which most have yet to recover. Only one African country, Botswana, has been consistently well governed since independence. Not coincidentally, average incomes in Botswana have grown faster than anywhere else in the world in the past 35 years, from bare subsistence to over $3,000 a year. But only one African in 400 lives in Botswana.

The short answer to the second question is that many individual Africans are working hard to better their own lot, but their rulers are prone to getting in their way. Too many governments are predatory, and not enough are competent. On the plus side, the continent has grown more democratic since the end of the cold war, raising hopes that African governments will become more responsive to their people's needs. That is very welcome. But, as Africans say, you cannot eat democracy. The real test is whether democratic governments will be able to lay the foundations for economic growth.

A few African countries are growing rapidly. Leaving aside those that have enjoyed sudden oil windfalls, the best performers are Mozambique, Rwanda and Uganda, which notched up growth rates of 12%, 9.7% and 6.2% respectively in 2002. All three countries have been doing well for a decade or so, and all three can plausibly claim that this is a result of better governance. The catch is that all three are growing from the lowest base imaginable, having suffered cataclysmic civil wars. All three have been given torrents of aid—between 50% and 70% of the national budget—to help them rebuild. None has yet regained its (modest) pre-war prosperity, and Rwanda's growth slowed in 2003.

Some African presidents, led by Thabo Mbeki of South Africa and Olusegun Obasanjo of Nigeria, are promoting a grand pan-African plan to promote better governance, attract more aid and boost growth. Most of the proposals obviously make sense: who could be against less corruption or better telephone links? But the plan will work only to the extent that individual African governments take it seriously.

Power in Africa today resides with national governments. Africa's nation-states may be artificial creations of the colonial era, but no one has the stomach to re-draw Africa's borders, so the continent is stuck with them. Progress, if and when it comes, will come country by country. The best-governed places will probably grow fastest, so African politicians must get the basics right: spend within their means, pass sensible laws and see that these are enforced even-handedly. Until they do, nothing else will move.

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The rule of big men or the rule of law?

Jan 15th 2004
From The Economist print edition

The wait for better governance could be long

Reuters

Mr Mugabe explains the secret of failure

THREE old judges sat in an empty courtroom, waiting for a case. They had time to talk: this was a traditional, informal court. “We used to gather under a tree,” said Bernard Setshedi, the chief judge. “The king would sit there all day, people would bring their problems, and he would make judgments.” There were no written laws, just traditions, understood by all and enforced by the king.

Then the tribe, the Bafokeng of South Africa, made a fortune from the platinum in its ancestral soil. The king built a brick courthouse and appointed some full-time judges from among the tribal elders. The surroundings look modern, but the traditions the judges uphold have not changed much from the old days.

“We tried a case today where one woman said her neighbour had sworn at her. We called a witness and found it wasn't true, so we threw the case out. It lasted 15 minutes.” The court deals with petty theft, marital problems and anti-social behaviour. Under South African law, it can hand down fines, but not punishments such as whippings (once a staple of customary justice) or jail terms. Serious crimes such as rape or murder must be turned over to the formal justice system.

Traditional courts have several advantages. Barney Mokgatle, one of the king's staff, explains: “It's better than going to town, queuing for ages and paying a lawyer money you don't have. It's quicker, cheaper, and less confrontational. We try to solve quarrels. If a man is having an affair, we try to show him that he has brought sadness into his house. It's about building relationships, not winning.”

Customary law is somewhat arbitrary, as it depends on unwritten rules and the whim of an unelected chief. But although the rules are unwritten, people are familiar with them and respect them. A traditional African chief may be unelected, but he is not wholly unaccountable. He lives in the same village as his people and hears their complaints. If he rules badly, he can be deposed, usually without bloodshed.

What traditional law cannot do is cope with the complexities of the modern world. You cannot have an unwritten banking code, or regulate telecoms by fiat. What works for simple local matters does not work for nation-states. And this brings us to one of Africa's greatest problems.

Before European colonists arrived, Africa was divided into several thousand kingdoms and chieftaincies whose systems of government had evolved over hundreds of years. By the time the Europeans left, they had squeezed the whole lot into a few dozen nation-states, whose borders cut some tribes in half and lumped others together with neighbours they did not much like. On to this artificial structure were grafted systems of government that mimicked European models.

Parliamentary democracy is a fine system, but it was alien to Africa. A bureaucratic state on the European model can function only if there are educated people to run it. But at independence Tanzania, for example, had only 16 university graduates.

Africa's first experiments with democracy did not last long. Elected governments quickly turned authoritarian or were swept aside by the army. The new regimes proved dysfunctional and unstable. In 1960-79, a total of 59 African rulers were toppled or assassinated. Only three retired peacefully, and not one was voted out of office (see table 2). Before long, most African countries had leaders who ruled as arbitrarily as traditional chiefs, but were far less accountable. A peasant could walk up to his chief's hut

and ask him questions; getting to talk to the president in his walled palace was a lot more difficult.

Some of Africa's new rulers called themselves socialists, others capitalists, but they often had more in common with each other than these labels suggested. Most concentrated as much power as they could in the presidency, and used it to enrich themselves and their supporters. Mobutu Sese Seko, ruler of Zaire (now Congo) from 1965-97, was the archetype. Bluntly declaring that "democracy is not for Africa", he ruled by decree, jailed his opponents, grabbed foreign businesses and shared them out among the elite. Lesser officials followed his example. From the fattest minister to the humblest clerk, anyone with power tried to turn it into cash. The regime even forged its own currency: the contractors printing bank notes for the government were caught producing more than one note for each serial number, and trousering the duplicates. Not surprisingly, inflation hit 9,800% in 1994.

A nice job, but not a safe one 2

How African leaders left office

	1960 -69	1970 -79	1980 -89	1990 -99	2000 -03	Total
Overthrown in coup, war or invasion	27	30	22	22	6	107
Died of natural or accidental causes	2	3	4	3	0	12
Assassination (not part of coup)	1	1	1	2	0	5
Retired	1	2	5	9	2	19
Lost election	0	0	1	12	6	19
Other (interim or caretaker regime)	6	8	4	14	1	33

Sources: "Risk, Rule and Reason in Africa" by Arthur Goldsmith, Harvard University; *The Economist*

The same sort of thing, although usually in less extreme form, was repeated all over Africa. The cleverest people either emigrated or went into government and devoted their energies to extracting rents from their productive compatriots. Politics became a zero-sum game. If you were in power, you would grow rich and your kinfolk would get more jobs in the civil service. If you lost power, you were in trouble. Of the 107 African leaders overthrown between 1960 and 2003, two-thirds were killed, jailed or driven into exile. This combination of risks and rewards gave African leaders a compelling reason to cling to power. They gagged the press, banned dissent and turned the security services into their private militia.

Enough is enough

Rule by big men rather than by law has been a disaster for Africa, but it cannot last forever. Urban Africans, who are better informed and harder to intimidate than peasants, are sick of being pushed around and are hollering for better government. Their numbers are rising, from 23% of Africa's population in 1980 to 35% in 2001, so their views are getting harder to ignore.

Foreign aid donors are also pushing for reform. Now that the cold war is over, they are less inclined to bankroll African despots for strategic reasons. Most of them insist that governments become more democratic and introduce liberal economic reforms. If African governments want the cash, they have to listen.

Since the mid-1980s, every African country bar the inaptly named Democratic Republic of Congo has held elections of some sort, and even Congo is due to go to the polls within a couple of years. Granted, many African elections are phoney. In Swaziland, elected MPs have no powers other than the right to advise the unelected king. In most countries, the ruling party uses all the apparatus of the state to buoy its re-election campaign. Public radio blares out its propaganda, public money pays for bags of grain to hand out to voters on polling day, and the police arrest opposition activists for holding meetings without permits.

No incumbent African leader ever lost an election until 1982, when the people of Mauritius booted out their prime minister. That was it for the 1980s, but 12 African leaders were voted out in the 1990s, and 11 since then. Their replacements were often just as bad, but sometimes obviously better, as in South Africa in 1994.

Several African countries are now less frightening places than they were. In Nigeria, for example, dissidents no longer fear being arrested and tortured since the death of the dictator Sani Abacha in 1998. The media have become freer in most parts of the continent: the number of boisterous private radio stations and newspapers has shot up in the past decade.

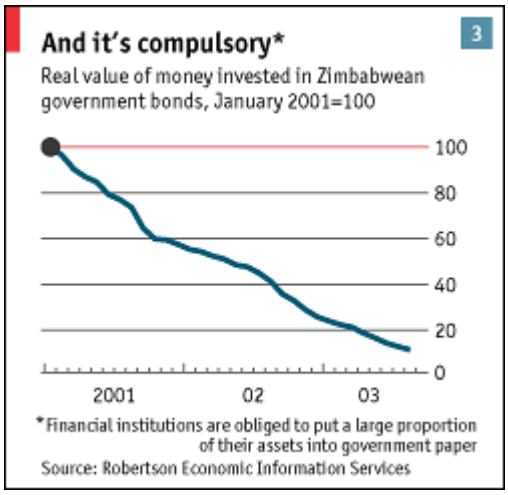
However, greater freedom has yet to spur greater prosperity, despite a sharp increase in the number of African governments that have embarked on liberal economic reforms. Such reforms were usually undertaken under duress. Decades of misrule had left most African governments flat broke, so they often agreed to do whatever the IMF asked—balance the budget, privatise, deregulate, whatever—in return for a bail-out. The results have been dismal. Africa is poorer now than when the reforms began. This failure

is trumpeted by anti-globalisers as proof that market forces are bad for developing countries. Liberal economists, on the other hand, tend to blame the grudging and haphazard way reforms were implemented.

Reform cannot work unless the people in charge actually want it to. But few African rulers have *laisser-faire* instincts, not least because anything that reduces their ability to make arbitrary decisions reduces their powers of patronage. George Ayittey, a Ghanaian economist, argues that most IMF-sponsored reforms have “amounted to reorganising a bankrupt company and placing it, together with a massive infusion of new capital, in the hands of the same incompetent managers who ruined it in the first place”.

The electorate has not shown much support for liberal reforms either. This is partly because they tend to cause short-term pain, as when subsidies are withdrawn or workers at state-owned firms are laid off. Some voters have even grown accustomed to corruption, and ask only that they should receive a cut. “The populace expects to exchange political support for concrete help,” says Jean-Pascal Daloz, a French academic. “That is the only way in which politics makes sense to them.” Often, this means they vote for a member of their own tribe, on the assumption that he will be more likely to share with them what he snaffles from the treasury.

Some electorates are more sophisticated than others. The voters of Zimbabwe, for example, are relatively well educated (thanks in part to Robert Mugabe's progressive education policies in the 1980s), which is why, now that Mr Mugabe is no longer popular, he has had to take such extreme measures to stay in power. In less than five years, he has cowed the judiciary, smashed most of the independent media, stolen two elections, dispossessed Zimbabwe's most productive citizens and printed money until inflation, though not at Zairean levels, has robbed savers and pensioners of almost all their assets (see chart 3).



The best thing that can be said about Zimbabwe's collapse is that it is one of a kind, at least in African countries not at war. Mr Mugabe has tried to disguise his contempt for the law (for example, by bringing in new legislation to authorise his land grab), which suggests that Africans have higher expectations of their leaders now than they did 20 or 30 years ago. Mr Mugabe may be murderous, but not on the scale of, say, Idi Amin in Uganda in the 1970s. And at least he pretends to hold free elections; Mobutu never bothered.

On the negative side, other African leaders have given little sign that they disapprove of Mr Mugabe. Several were upset at the way Zimbabwe was suspended from, and eventually quit, the Commonwealth. South Africa's president, Thabo Mbeki, has promised America's President George Bush that the Zimbabwean crisis will be solved this year. But Mr Mbeki is not under pressure from his own electorate to do anything drastic. Themba Khumalo, news editor of the *DailySun*, South Africa's most popular black paper, says his typical reader has met refugees from Zimbabwe, and would not want to see South Africa go the same way. “But on the other hand, they think [Mugabe] is a hero, that he's sorting them [the whites] out.”

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Breathing life into dead capital

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Why secure property rights matter

Panos

Not much use as collateral

YOUR correspondent once asked a Somali nomad how much his house cost. The nomad found the question slightly baffling. He explained that he had built it himself, with materials he had to hand. The walls were made of sticks, woven together and curved into a dome. For protection against rain and sandstorms, he had laid animal hides over the top and lashed them down. He could not say how much the dwelling was worth, because it would never have occurred to him to sell it. When he moved away in search of better pasture, he simply dismantled his house, loaded it onto a camel's back and took it with him.

Such a lifestyle requires a lot of space. When their cows have stripped one area of grass, nomads simply move on. But as Africa's population grows and farmers encroach upon nomads' traditional grazing grounds, the wandering herdsmen are being squeezed into ever smaller and more arid pockets of territory. They will be able to defend themselves for a while—young male nomads in Somalia, Ethiopia and Kenya all seem to carry submachineguns—but in the long term, their lifestyle is probably doomed.

For settled Africans, however, there should be more than enough land to go around. The continent is only one-25th as densely populated as East Asia. But Africans find it hard to use what they have to best advantage because they lack secure property rights. Very few can prove that they own their land or their homes, because they do not have title deeds. This matters, because without a reliable system for ascertaining who owns what, assets cannot be used as collateral.

In rich countries, if a farmer wants to invest in better seeds or bigger tractors, he can probably borrow the necessary cash using his land as security. If he fails to honour his debt, the bank takes the land. If all goes well, however, his easy access to credit allows him to make his land more productive, which in turn increases its worth. Asset-backed lending is a crucial element in the dynamism of advanced capitalist countries. In America, for example, the most common way for an entrepreneur to raise start-up capital is by mortgaging the family home.

In Africa, this is much harder. Less than 10% of the continent's land is formally owned, and barely one African in ten lives in a house with title deeds. Farmers and urbanites, unlike nomads, usually have a clear idea what their homes and maize-plots are worth. For example, in Mtandire, a Malawian slum, a sturdy brick bungalow costs about $300. That is a large sum by Malawian standards: nearly twice the average annual income. But home-owners in Mtandire have enormous trouble making their assets work

for them.

One explained that she wanted to borrow $200 to expand her goat-slaughtering business to meet a ravening demand for goat stew, but no bank would accept her house as collateral. Like the other houses in Mtandire, it was built on “customary” land. She had bought it from peasants who had farmed it for generations. The only proof that they had owned it was the say-so of the village chief. Banks need more surety than that, so the home-owner's butchering business seems likely to stay small for the foreseeable future.

Multiply this story by several million, and it is clear that Africans are sitting on a colossal stock of underexploited assets; what Hernando de Soto, a Peruvian economist, calls “dead capital”. Mr de Soto estimated that the total value of Africans' informally owned houses and farmland in 1997 was roughly $1 trillion. That is nearly three times sub-Saharan Africa's annual GDP, and more than 70 times the amount of aid the continent receives each year.

Sound property rights have great advantages. When people are confident that they will not suddenly be dispossessed, they are more inclined to make long-term investments, such as extending the family home or buying a new plough. Property rights promote flexibility, too. They allow peasants who want to move to the city to look for work to sell their land, or to rent it out without fear of being unable to get it back later.

Transparently useful

In rich countries, property registries provide a wealth of commercially useful information. They show who owns a piece of land, where the boundaries are, and whether it is legal to build a factory on it. Such information makes it easier to spot commercial opportunities, and gives strangers confidence to do business with each other. Buyers know what they are buying. If someone cheats them, they know where to send the bailiffs.

In most African countries, by contrast, registries cover only a small fraction of fixed assets. Most Africans, being outside the formal system of rules and paper, prefer not to risk buying anything they cannot see. So farmers have to take their maize crop physically to market and usually have to sell it straight away, even if the prices are low, because they cannot afford the truck fare back. Western farmers can sell promises to deliver crops they have not yet planted, which is less cumbersome and better for the cashflow.

Many African peasants are aware that they lack property rights, and resent the fact. A survey in Zambia found that, despite the country's low population density, nearly half the farmers questioned felt that their land tenure was insecure. These farmers said they were willing to pay an average of $40 for more secure tenure. Several African governments have also realised that better property rights would help their citizens prosper, and have passed laws seeking to formalise customary tenure. This is a good first step.

Obviously, secure property rights cannot be established overnight. In the West, they evolved over centuries. And Africa cannot simply adopt rich countries' rules, because its governments do not have the expertise to enforce them, except perhaps among small enclaves of their better-off citizens. For example, other things being equal, it is desirable for land to be accurately surveyed before being registered. But there are never enough surveyors in Africa, and their services are too expensive for the poor. In Zambia, surveyors' cartels artificially restrict the number of surveyors who may practise, leading to backlogs of up to seven years. So if property rights are to be extended to the maximum number of people, the system has to start rough and cheap; it can always be polished later. And if it is to be accepted by ordinary people, it must build on arrangements they know and trust.

Mozambique's story is instructive. During the 1970s and 80s, property rights did not exist there. A Marxist government had abolished them in theory, and a vicious rebel movement had destroyed them in practice in all the areas it ravaged. Some 5m people—a third of the population—were driven from their homes, and their fields were sown with landmines.

After the war ended in 1992, however, the (now ex-Marxist) government was able to resettle those 5m people astonishingly quickly. Land records were rudimentary or non-existent, so the government relied on local institutions to resolve the inevitable disputes. The state still owns all the land, but families' occupancy rights were codified in law in 2000, and investors can now buy long leases. Those who want to lease unoccupied land, of which the country has a lot, have to negotiate with neighbouring communities,

which reduces the likelihood of anyone being unjustly dispossessed.

The system is far from perfect, but it is not bad for a country where the average citizen earns only $200 a year. Better property rights have fostered confidence, and therefore investment. Economic growth in Mozambique has been in double digits in four of the past six years. Such successes have been too rare, however. A recent study of 19 African countries that had passed laws to upgrade customary tenure found that eleven had done absolutely nothing to put these laws into practice.

Overall, since independence, African governments have tended to weaken property rights rather than strengthen them. The European colonists, for the most part, had preferred to leave customary land arrangements alone, except in areas where they themselves wanted to live or establish plantations. After liberation, however, several African governments declared a state monopoly over the ownership or allocation of land. This took power away from local chiefs and bestowed it on bureaucrats. In the absence of checks and balances on central power, this proved disastrous.

Ethiopia provides an illuminating example. Within living memory, the country has suffered both feudalism and Marxism. In the 1970s and 80s, peasants were forced at gunpoint into giant collectives, causing production to collapse and paving the way for the great famine of 1984, in which 1m people died. Since 1991, when a less oppressive regime seized power, harvests have been up again and droughts less lethal. But the feudal system of imposing heavy taxes on subsistence farmers remains, as does the Marxist notion that the state should allocate all the land.

Peasants' rights over the ground their families have tilled for generations are conditional on them living on or near it. Owners who have not cultivated their farm for two seasons risk having it confiscated. This ties them to a location and a way of life that offer little hope of advancement. Even the most ambitious think twice before seeking their fortune in the city, because if things do not work out they may have nowhere to return to.

Establishing sound property rights is a long and tricky process, but dismantling them is quick and easy. Think of Zimbabwe, which until the late 1990s had a large and sophisticated formal sector. Since Robert Mugabe started gleefully tearing up title deeds, Zimbabwean industry has all but collapsed.

A qualified welcome

Another, less remarked example is Côte d'Ivoire. Under the fairly benign dictatorship of Félix Houphouët-Boigny, migrants from neighbouring countries, such as Burkina Faso, were welcome to come and grow cocoa in Côte d'Ivoire. They arrived during an economic boom, when many young Ivorians were migrating to the cities to take up paid jobs. But when the boom turned to bust, many of the city-dwellers lost their jobs and went back to their villages looking for land to cultivate.

In the absence of clear title, squabbles erupted. Tensions between native Ivorians and Burkinabe planters were already high when a law was passed in 2000 under which all customary land not converted to full title within ten years would revert to the state. It was obvious from the outset that most claims would not be processed in time. Burkinabe planters feared that they would lose their land. Many did: land grabs became common, often with the connivance of the police and officials. Within two years, these and other quarrels had snowballed into civil war.

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Coping with conflict

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Wars have crippled Africa, but peace is possible

EPA

Shouldn't you be in school?

IN 1999, a fifth of all Africans lived in countries battered by wars, mostly civil ones. Since then, things have improved. Hideous conflicts in Sierra Leone and Angola have stopped, as has the pointless border clash between Ethiopia and Eritrea. Liberia's warmongering ex-president, Charles Taylor, has been pushed into exile, Congo's rebels and government have signed a peace pact and Sudan's are set, with luck, to do something similar. Whether this is a new trend or a brief lull remains to be seen. New wars sporadically erupt, for example in Côte d'Ivoire, a once-stable country that appears to be sleepwalking into catastrophe. And some of the conflicts that are supposed to be finished may turn out not to be, for their underlying causes are often yet to be resolved.

Each conflict has its own unique and complex set of causes, but some generalisations can be made. A study of the world's civil wars since 1960 found that the most important risk factors were poverty, low economic growth and a high dependence on natural resources, such as oil or diamonds. Africa's wars certainly seem to support this theory.

Take Congo. After some 3m deaths between 1998 and 2003, its war is supposed to be over. The neighbours who invaded Congo have mostly pulled out, the main rebel leaders have joined a transitional government in Kinshasa, the capital, and elections are supposed to be held in the not-too-distant future. But in the east of the country, dozens of micro-wars smoulder unchecked. The combatants are mostly irregular militias, and their victims are mostly unarmed civilians.

In many areas, villages are plundered so often than peasants are afraid to sleep in their huts at night. Some hide in the bush, others seek sanctuary in the nearest garrison town. Zihalirwa Barnaba, for example, leaves his village before dark every night and walks for 90 minutes to the safe-ish town of Walungu, where he sleeps in the street. Every morning, he gets up and walks all the way back to his fields. This wastes precious time and energy he needs for growing food. “I can't possibly grow enough to eat,” he says.

The alternative is often worse, however. Gunmen burst into Charlotte Nyamugali's hut one night and made her help them carry off her belongings: “Pots and pans, clothes, everything.” Then they beat her and gang-raped her. She managed to escape, but two months later more gunmen came and stole everything that the first group had missed.

Millions of Congolese lead similarly fearful lives. In the north-east, militias are trying to exterminate whole tribes. Throughout eastern Congo, rape, including male rape, is routine. Some guerrillas carry little bottles of palm oil, in case.

How did Congo get in this mess? It is a long story. To oversimplify: after independence in 1960, Congo was ruled so corruptly that the state atrophied. Unpaid officials stopped even pretending to carry out their duties. Soldiers took to robbing the citizens they were supposed to protect. By the 1990s, this huge country was so weak that its tiny neighbour, Rwanda, was able to walk in and topple its government.

Rwanda is currently ruled by those who stopped the genocide in 1994. The president, Paul Kagame, is a tough former bush-fighter, who has helped to overthrow five governments in three countries. When the Hutu killers responsible for the genocide fled into Congo (then called Zaire), Mr Kagame pursued them. When Mobutu Sese Seko, Zaire's dictator, armed and succoured the Hutus, Mr Kagame organised a

rebellion and ousted him.

In his place, the Rwandans installed Laurent Kabila, a veteran Congolese guerrilla they hoped would help them flush out the *génocidaires* hiding in Congo's rainforests. Instead, he recruited them into his army. So the Rwandans invaded again and would have toppled Kabila, too, had he not been saved at the last minute by the armies of Angola and Zimbabwe.

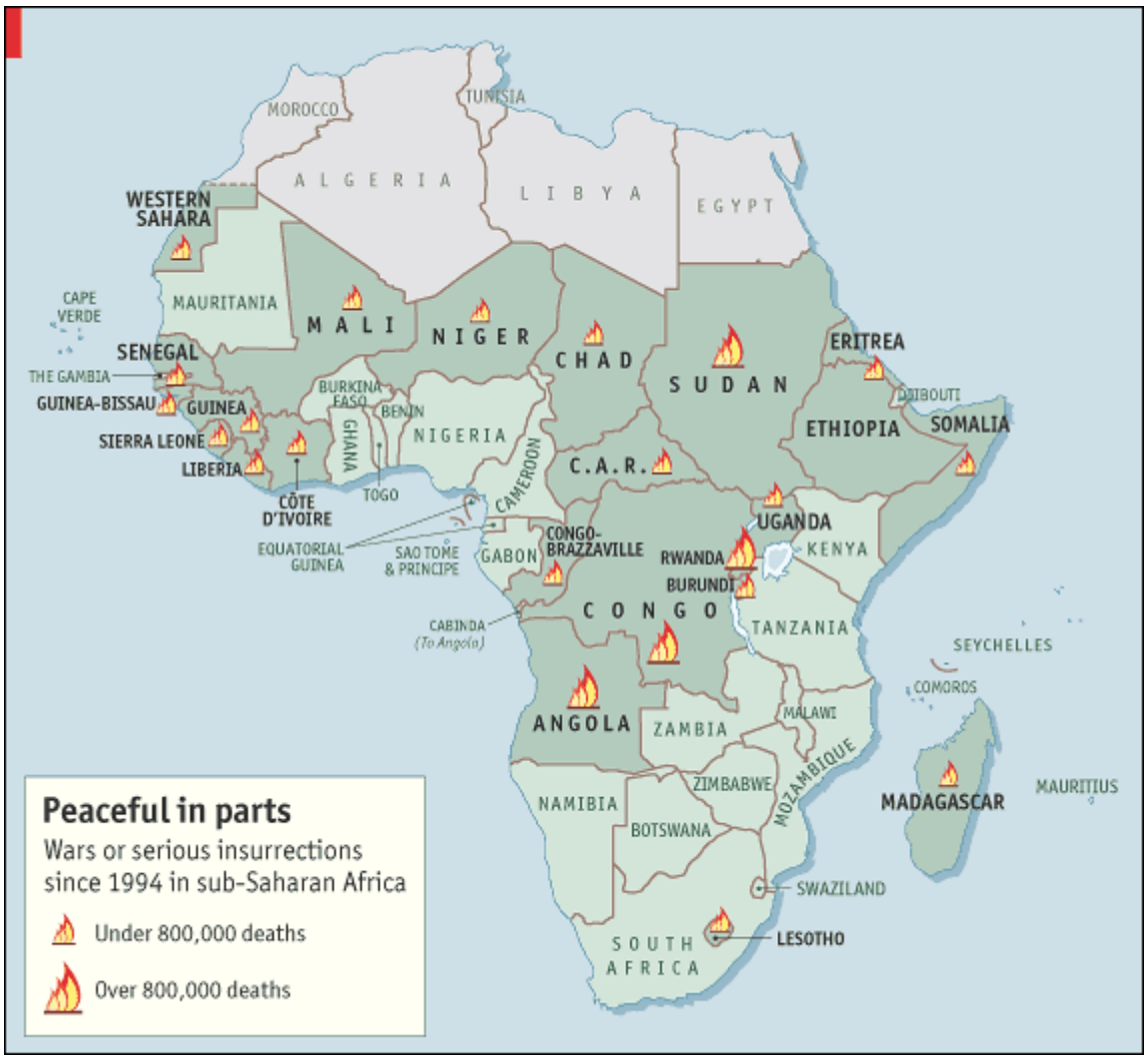
The war then entered a stalemate. All the foreign armies provided local militias and rebel groups with arms to do their fighting for them, and set about looting Congo's minerals. After five years, exhaustion and international pressure forced most of the foreigners to withdraw, and the two larger rebel groups to strike a peace deal with the Congolese government. But dozens of smaller militia bands remain at large, killing and looting because that is how they eat.

Lessons in survival

Amid all this chaos, ordinary Congolese show admirable resilience. “You have to hustle to get by,” goes a local song. Vendors set up shops in rusty shipping crates or the shells of broken-down minibuses. Peasants earn extra cash by carrying things. Thousands can been seen trekking along the mountain roads that lead to the town of Bukavu, with cabbages, fish or furniture on their heads. One “transporteur” says that a typical day's work involves walking for four hours into town, buying a 20-litre jerrycan of petrol, and humping it for six hours back up the mountain to his village, where his wife sells the petrol. Their profit margin? The jerrycan.

Civil servants in Bukavu have not been paid for more than a decade, so they all have sidelines. Jean-Pierre Mihigo Chako, a teacher, also runs a bar. He has had to learn how to fend off tax collectors sent by the rebel group that controls the town, who try to charge him for every chair, for playing music, and even for having a sign over the door. “I won't die of hunger,” he shrugs. But he would much rather be teaching sociology.

Large swathes of Africa are stuck in a vicious circle (see map). They are prone to war because they are poor and badly governed. Wars make them poorer still, and the leaders who rise to the top during wartime are rarely benign.



Most of the things African governments can do to reduce the risk of war are worth doing anyway: govern well, spend money on schools rather than soldiers, allow space for peaceful dissent, and avoid inflaming ethnic grievances. Peacekeepers, and peace enforcers, also have a role. Non-Africans, ashamed at their failure to halt Rwanda's genocide, have done more in recent years. The British helped stop Sierra Leone's war, the French are policing a shaky ceasefire in Côte d'Ivoire, and the UN is struggling to calm Congo, among other places.

Some of the more settled African countries would like to play a greater part in stabilising their neighbours. The African Union (AU, the successor body to the Organisation of African Unity, OAU) wants to create a “rapid-reaction” force to stop wars before they blaze out of control. The plan is that by 2010, each of five regions will have a brigade, under AU command, that will be ready to rush to trouble spots at short notice. It is a brave attempt to tackle a real problem: peacekeepers dispatched by the UN Security Council do not usually arrive until three to six months after the event.

But much more money is needed. The AU has earmarked less than $6m a year for the project. Even assuming that the member states all cough up, which they have not done in the past, this barely buys a hubcap for the proposed continental fire engine. By way of comparison, the OAU spent $7.2m keeping a mere 67 military observers in Burundi between 1993 and 1996. The UN spends $1.3 billion a year on peacekeeping in Africa, with mixed results.

With outside funding, the plan might still work. An African force ought to be cheap: its soldiers would not need to be paid at blue-helmet rates. They should also arrive more quickly, because they would be nearer to start with. An African force could be reasonably effective if it were built around the best armies in the region: South Africa's and Nigeria's. The UN might find that, by sub-contracting some of its African peacekeeping chores to the AU, it would stop more bangs for its buck. But first the AU would have to show that it is serious about solving Africa's problems; something its predecessor never was.

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Love and death

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Belatedly, Africans are taking AIDS seriously

Magnum

A wretched job, and then you die

WITHOUT a word, the young woman leant back against the bonnet of a parked car and lifted her miniskirt. The group of men opposite smiled but showed no interest, so she pushed her skirt back down and sauntered off. It was late evening, and Nairobi's pavements were bustling with prostitutes. It is a miserable job, and usually lethal. More than 85% of Nairobi's sex workers are thought to be HIV-positive.

AIDS has hit Africa like a never-ending hurricane. According to the UN, whose figures are rough but the best we have, between 25m and 28.2m Africans carry HIV, the virus that leads to AIDS. Some 3m-3.4m were freshly infected last year, and between 2.2m and 2.4m died. In much of southern and eastern Africa, between a fifth and a third of adults are infected; in Botswana and Swaziland, a staggering 39% are. In several of the worst-affected countries, HIV prevalence appears to have levelled off, but this is no cause for joy. It reflects not a reduction in the rate of new infections but an increase in the death rate.

The human consequences of AIDS are appalling. In several African countries, most young people will probably die of the disease, often after much suffering, and often in the knowledge that their loved ones will soon die, too. Graveyards are expanding in all directions, and tombs are overrun with weeds because the living are too weak to tend them. The disease aggravates Africa's famines. Hunger and AIDS separately reduce the body's defences against disease, but the two curses reinforce each other. Hungry, immuno-compromised people fall sick, and sick people are often too weak to grow enough food.

The broader economic impact of AIDS is hard to predict. Most experts think that the epidemic will reduce overall growth by no more than a percentage point each year. Mass death could actually make life easier for those who survive, because there will be more land to go around. Labour could become scarcer and command a higher price, as happened in Europe after the Black Death.

Other forecasters are more worried, however. AIDS is not like the bubonic plague: it strikes mostly those of bread-winning age, and it kills them slowly. Sick workers produce less. Afflicted families exhaust their savings buying drugs. Daughters drop out of school to care for stricken parents. With so many Africans' immune systems ravaged, debilitating diseases that seemed to be under control, such as malaria and tuberculosis, are spreading again. If AIDS is not checked, it could make Africa much poorer in the long term. When people do not expect to live long, they tend to invest less in the future. They save less, and are less likely to risk setting up a business. They are also less likely to send their children to school. A study in Côte d'Ivoire found that households afflicted by AIDS halved their spending on education. Huge numbers of children lose their parents, and often their teachers, too, so the transmission of knowledge between generations is interrupted.

Aunts and grandmothers often take in their orphaned nephews and grand-daughters, but the more orphans AIDS creates, the more strained Africa's extended-family networks will become. Governments may try to subsidise the education of children from families crippled by AIDS, but will find it harder as the disease kills more taxpayers, teachers and administrators. Pessimists predict that AIDS will steadily erode Africa's stock of human capital, causing productivity to tumble. Children who grow up ignorant will end up poorer, and less able to educate their own children.

Africa cannot afford to lose skills; it has few enough to start with. A recent study predicted that unless

the government moved quickly to tackle AIDS, South Africa's economy would collapse within four generations. On the other hand, if South Africa acts on an ambitious plan, announced last November, to give anti-AIDS drugs to those who need them, its prospects look less dire.

AIDS probably makes Africa even less stable politically than it would be without the disease. Lacking parental guidance, orphans sometimes drift into crime. Young men who expect to die young may become more reckless, and so more likely to join a criminal gang or a rebel army.

Africa's instability, in turn, probably promotes the spread of AIDS. Between 40% and 60% of the foreign soldiers who fought in Congo's war were HIV-positive. After five years of Rwandans, Ugandans, Zimbabweans and Angolans marching through Congolese villages, scientists have observed a frenetic mix of different HIV sub-types in local bloodstreams, which could cause new drug-resistant strains to develop.

Why Africa?

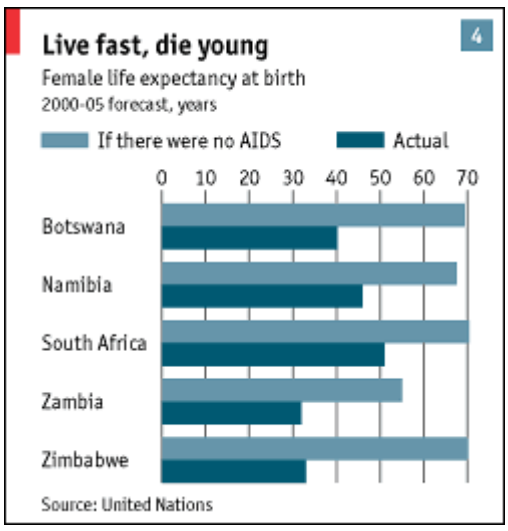
Why has AIDS blighted Africa like nowhere else? For many reasons. Poor people cannot afford decent health care. Without antibiotics, they cannot treat other sexually transmitted diseases, so they often suffer open sores through which the virus can easily enter. Africa has a lot of migrant labourers, who spread HIV far and wide. The populations of some cities in eastern and southern Africa are disproportionately male, because so many men work away from home, often leaving their wives back in the countryside to tend the fields and look after the children. A lot of these migrant workers sleep with prostitutes, and then infect their wives when they go home. A survey in Zambia found that three in four wives felt they could not refuse sex with their husband, even if they knew he was unfaithful and HIV-positive.

Many Africans find it hard to talk about sex. Parents find it especially hard to be frank with their children. Some Africans even believe that westerners who go on about AIDS in Africa are accusing black people of immorality. Thabo Mbeki, South Africa's president, once complained that: “We are blamed as criminals and seen as human beings of a lower order that cannot subject its passions to reason...as natural-born, promiscuous carriers of germs, unique in the world, doomed to a mortal end because of our unconquerable devotion to the sin of lust.” This rather misses the point.

“How can we fight AIDS if we don't talk about sex?” asks Isabella Matambanadzo, who runs a women's-rights group in Zimbabwe. No one discusses the fact, she says, that because virginity tests are so popular in Zimbabwe, girls are having anal sex, which increases the risk of infection. Motherhood carries such a big premium (she cites the custom of burying a childless woman with a rat in her coffin to symbolise the missing offspring) that some women would rather be HIV-positive than childless.

Sexual mores vary widely within Africa, all the way from the strict Islamic code of Sudan to the more relaxed attitudes in, say, Zambia. No one can be sure what Africans are doing in bed or in the shade of a mango tree, but the HIV statistics themselves tell a story.

In Africa, unlike elsewhere, more women than men are HIV-positive, because the virus is transmitted mostly heterosexually, and women are more likely to be infected during vaginal intercourse than men are. Young African women—those in their teens and twenties—have a much higher chance of being infected than men of the same age, because they are sleeping with older men, who tend to have more money.



This pattern of sexual networking keeps the virus circulating among different generations. Male and female HIV rates equalise in the mid-thirties, as the women who caught it young die, and men get old and prosperous enough to start supporting younger mistresses.

So far, the countries that have curbed AIDS have succeeded largely by persuading people to avoid risky sex. This is not easy in a continent where no one wears a seat belt, but it is not impossible. In Senegal, the government nipped the epidemic in the bud by cajoling prostitutes into using condoms. Since 1990, HIV prevalence has stayed low and stable, at about 1%. In Uganda, after an

energetic campaign promoting abstinence, fidelity or the use of condoms, prevalence has tumbled from perhaps 30% to 5%.

In the future, drugs will play a larger role in the fight against AIDS. Westerners with HIV have for several years kept well by popping costly pills. What is new is that these anti-retroviral drugs have become much cheaper—with prices dropping by more than 95%—and that donors are increasingly prepared to pay for them. In 2002, only one HIV-positive African in 400 took anti-retrovirals. By 2005, the UN wants to see 3m people in developing countries taking the drugs, and most of these will be in Africa.

Such an ambitious plan will be hard to implement, given Africa's rudimentary health-care infrastructure, and the likelihood that drug-resistant strains of the virus will evolve. One of the drugs' unpleasant side effects will be greater dependency on aid. South Africa and Botswana, the two richest countries with huge epidemics, will be able to pay for their own drugs, but other African countries will not, even with deeper discounts. Millions of Africans will soon depend on donors for their lives; a cut in aid could spell carnage.

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Opportunities, mostly missed

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The risks and rewards of doing business in Africa

Reuters

Somehow, Africans get their produce to market

YOU hear them before you see them. Low, throaty grunts echo from either side of the path, but the forest canopy is too thick for you to spot the gorillas until you are in their midst. Your heart stops. And then the alpha male charges you. Your guide holds your shoulders to make sure you do not run away: that would be a mistake. The charging beast stops a few feet short of you and, his point made, goes back to munching fruit.

Few thrills match gorilla-watching, and there are few places where you can do it. The Kahuzi-Biega national park, near Bukavu, is one of the most beautiful. It has startling mountain views, a vast forest flecked with red and purple flowers, and an abundance of birds, butterflies, wild pigs and leopards. But no tourists, because it is in Congo.

Africa is a continent of squandered opportunities. Bukavu, a town of lakeside villas and throbbing nightclubs, was once a popular resort. It could be again, if something were done about the guerrillas in the forest, the chasms in the roads and the officials at the border who try to confiscate your passport “for security reasons”. Few parts of Africa have such a concentration of these ills as eastern Congo, but many have enough to scare off investors, both foreign and local.

Net private direct investment south of the Sahara was $3.9 billion in 2002—a paltry sum, and worse than in six of the seven previous years. Ah yes, retort optimists, but the return on foreign direct investment in Africa is higher than in any other region. The UN Economic Commission for Africa calculates that, for Africa as a whole, including North Africa, the average return on FDI is four times that in G-7 countries, and twice that in Asia. This is partly because the continent is considered so risky that investors will sink money only into ventures that promise big and quick profits. But it also suggests that the risks are exaggerated.

Most African countries are not at war, and most governments have grown more business-friendly over the past decade. More prudent fiscal policies have brought a much-needed improvement in macroeconomic stability: whereas in 1995, 28 countries had double-digit inflation or worse, in 2002 only 11 did. Almost all governments now say they want to see more private businesses flourish, though there is still what Ugandan president Yoweri Museveni calls an “anti-business bias” in many African bureaucracies.

Smart businessfolk can do well in Africa. Oil firms are flocking to explore the waters off the continent's west coast, and expect Africa to supply a quarter of America's oil imports by 2015. Mining firms dig for gold, cobalt and diamonds. Some non-extractive industries are booming too. Some 25m Africans have mobile telephones, up from virtually none a decade ago. Partly because there is so little competition, firms that make and distribute cheap luxuries, such as bottled drinks or branded soap powder, have prospered. Coca-Cola, for example, is Africa's largest private employer.

Even in Bukavu, there are two functioning factories. One makes beer, which sells well even in wartime, and the other, Pharmakina, produces 80% of the world's quinine pills. The Pharmakina plant was smashed and looted by Mobutu's fleeing army in 1996, but Horst Gebbers, the German manager turned part-owner, somehow rebuilt it. There are no banks in Bukavu, so his foreign customers pay into an account in Europe, and the firm has an arrangement with a local trader who advances it Congolese cash. “We make a small profit,” says Mr Gebbers, “and we don't get involved in politics.”

You do not hear much about such successes, not least because multinationals that do well in Africa tend not to advertise the fact. “Ironically, saying that we are doing well in Africa can have the effect of worrying investors,” laments David Hampshire, managing director of the thriving African arm of Diageo, a global drinks giant.

A simple way for African governments to promote investment, particularly the most useful, technology-transferring type, would be to privatise faster. Sadly, the pace of sales of state-owned firms has slackened, from 254 deals in 1997 to 19 in 2001. Governments have sold lots of little assets—state-owned hotels and the like—but clung doggedly to the big ones, such as telephone and electricity utilities. These are the ones they most need to sell, not only because they would raise more money, but also because these essential services have mostly fallen into disrepair in state hands and need investment, professional management and competition to revive them.

A typical African country has a GDP of $2 billion-3 billion, equivalent to that of a medium-sized town in a rich country. In China, firms can market to 1.3 billion people under one set of laws (or two, if you count Hong Kong). Africa's 700m citizens are scattered among 48 countries (or more, if you count the bits that have broken away from Somalia). So a pan-African investor faces a tangle of different regulatory systems, most of them cumbersome, capricious and subject to frequent change.

Consider what it takes to incorporate a new business in Africa. This should be simple: it requires the new firm to be registered for tax and for statistical purposes. In rich countries, it is indeed quick and cheap: in Australia it takes two days and costs the equivalent of 2% of the country's average annual income per person. There are no minimum capital requirements. In Congo, by contrast, it takes 215 days, costs close to nine times the average annual income per person, and firms must start with a minimum paid-up capital of more than a third of that preposterous fee.

In Africa as a whole, the average cost of registration is nearly twice the average annual income per head. The rules that make it so expensive for a business to get started are often pointless. In francophone Africa, for example, registration usually requires notaries and judicial approval. In Ethiopia, a firm has to place a costly announcement in the state-owned press. Other rules purport to have a social value, but are actually counter-productive. A Ghanaian firm wanting to register must spend 90 days doing an environmental audit of its business plan. The net effect of this rule is probably more pollution, because many firms would rather remain unregistered and unregulated than incur that sort of cost.

Contracts are a problem, too. In Singapore, it takes about 50 days to enforce a simple commercial contract through the courts. In Angola, it requires 46 steps and takes 865 days to enforce a similar contract. No prizes for guessing which country has the better reputation for probity. In Malawi, the cost of recovering a $100 debt through the courts is close to $900, so Malawian businessfolk tend to deal only with people they know. This is true all over Africa: a survey in Cameroon, Côte d'Ivoire, Kenya and Zambia found that firms bought on average 70% of their supplies from a single supplier, with whom they had typically dealt for a decade.

The evidence that over-regulation stifles growth is so compelling that most African governments now say they want to simplify things. Ghana and Tanzania, for example, have set up fast-track courts. Tanzania's, which deals only with large commercial disputes, allows firms to pay a premium to have their cases processed in 3-4 months rather than the usual 2-3 years. South Africa has streamlined company registration, tidied up the tax code and trimmed its protectionist thicket.

But in several African countries those regulations are proving to be hydra-headed. The more onerous

they are, the more likely businesses are to offer bribes to get round them, so lawmakers have a perverse incentive to keep inventing new ones, even as the old ones are hacked away. Nigeria, for example, is forever banning and unbanning imports such as fruit juice. The Zimbabwean government periodically, and vainly, tries to fix the price of everything from bread to paraffin.

The right to trade

The usual way for poor countries to get rich is by exporting, so the collapse of the world trade talks last year has seriously harmed Africa's prospects. African goods sold in OECD countries (ie, rich industrialised ones) face tariffs roughly ten times higher than those levied on goods traded within the OECD. Barriers are steepest in areas where Africa, with its vast amount of land and relatively cheap workers, has a comparative advantage, namely agriculture and textiles. Rich countries subsidise their farmers to the tune of $320 billion a year, a sum not far short of Africa's annual GDP. Combined with high tariffs and small quotas for some farm products, this makes it dauntingly hard for African farmers (and remember, most Africans are farmers) to export to rich countries.

Trade barriers within Africa have come down; the average unweighted tariff is now 16%, compared with about 30% in 1990. But African countries that have cut tariffs have often erected other barriers, such as discriminatory taxes on imported products, that provide nearly the same degree of protection.

And not all trade barriers are of the legal sort. Bad roads and obstructive officials hinder trade at least as much. A Cameroonian beer truck on which your correspondent once hitched a ride took four days to cover 500km (310 miles), not least because it had to stop 47 times for bribe-hungry policemen at road blocks. And that was without crossing any borders.

There is one group of investors that is showing considerable interest in Africa. With sanctions gone, South African firms now invest more in the rest of Africa than companies from anywhere else: about $1 billion a year since 1994, in everything from mobile telephones to supermarkets.

Why are they doing it? Partly because African assets are cheaper than European ones; but also because they see opportunities, and because they think they know how to do business in Africa. It is a two-way street; many professionals and entrepreneurs from elsewhere in Africa are heading for the sleepless lights and smooth roads of Johannesburg. If any country can set an example to the continent, it is South Africa.

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An addictive lullaby

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Can aid spur development?

THE World Bank once offered loans to promote cocoa farming in Equatorial Guinea. Government ministers immediately seized the best cocoa farms and spent the loans on fancy cars. This is typical of how Africa's unpayable debt was incurred. For every dollar that foolish northerners lent Africa between 1970 and 1996, 80 cents flowed out as capital flight in the same year, typically into Swiss bank accounts or to buy mansions on the Côte d'Azur. Africans today are still paying for their old rulers' profligacy. Since the late 1990s, debt relief has eased the burden a little, but a recent IMF study predicted that the current multilateral debt-relief programme would not be enough to bring Africa's debts down to "sustainable" levels, and suggested that rich countries offer more grants.

Attempts by outsiders to help Africa have an inglorious record. Development aid was supposed to promote growth, but has conspicuously failed to do so. Extravagantly aided poor countries have grown no faster than unaided ones. In the 1990s, donors grew disillusioned and started to shut their wallets.

Then, in 1998, along came David Dollar and Lant Pritchett of the World Bank with a study that showed how aid could be made to work. They found that countries with sound economic policies (low inflation, a budget surplus and fairly free trade) and good institutions (rule of law, not much corruption, an effective bureaucracy) benefited from aid. Income per head in well-run countries grew a little if they received only a little aid, and by a lot more if they received a large amount of aid. By contrast, countries with bad policies and institutions stagnated or grew poorer, even with large handouts.

Virtue rewarded

Since then, it has been conventional wisdom that development aid should favour well-governed poor countries. This is the logic behind President Bush's promise of a 50% increase in American development aid by 2006, and behind the New Partnership for Africa's Development (NEPAD), a pan-African initiative that promises better governance and asks for more aid.

Some economists, however, have doubts. Mr Dollar's and Mr Pritchett's findings were based on data for the period 1970-93. William Easterly, a former World Bank economist, and others tried to update the results by using figures for 1970-97, but said they could "no longer find evidence that aid promotes growth in good policy environments". Ian Vásquez of the Cato Institute, a libertarian think-tank, thinks this may be because during the period covered by the first study several developing countries, such as Peru and Argentina, had carried out far-reaching reforms that yielded rapid growth. The second study included a period when they failed to stick with these reforms, and growth sputtered.

Mr Vásquez argues that over-rewarding these governments with aid may have dulled their incentive to continue with tough reforms because there was no longer a crisis to justify them. Both Mr Easterly and Mr Vásquez also doubt the World Bank's claims that it has made its aid disbursals more selective. According to its own figures, it currently gives more aid per head to countries with poor policies ($2.30 a year) than it did in 1990 ($2).

So what should donors do? More research would help. So would more private philanthropy. Individual donors are unlikely to bankroll despots for strategic reasons, as governments do. Bill Gates insists that the projects he supports through his private foundation should save the maximum number of lives at minimum cost, and monitors results more assiduously than state aid agencies seem to. Meanwhile, if western governments really want to help the poor, they should lift their trade barriers. "Aid without trade," says Uganda's president, Yoweri Museveni, "is a lullaby—a song you sing to children to get them to sleep."

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Africa's engine

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For the whole continent's sake, as well as its own, South Africa needs to do better

“SOUTH AFRICA is very welcoming,” says Trevor Ncube. Two years ago, Mr Ncube, a jovial young Zimbabwean businessman, bought the *Mail and Guardian*, a struggling South African newspaper, and turned it around. Given where he comes from, it is not surprising that he finds his new surroundings congenial. Back home in Zimbabwe, the two independent weeklies he owns are constantly harassed and threatened with closure. In South Africa, a publisher's worries are more mundane: advertising rates, circulation figures and tough competition.

Africans flock to South Africa for the same reason that Mexicans head for California. The country accounts for 45% of sub-Saharan GDP. “South Africa works,” says Mr Ncube, and he is right. This becomes apparent as soon as you step off the plane. Johannesburg's airport is gleamingly first-world. The people behind the desks at passport control are courteous and efficient. Wave your plastic at Avis or Budget, and in no time you are speeding into town in a locally built Toyota. The phones connect, the wine is delicious and you are free to do pretty much what you want. Other Africans are envious.

In some ways, South Africa's recent history has been inspiring. Only ten years ago, 90% of its people were denied full citizenship. At the height of apartheid, blacks were barred from good jobs, schools and neighbourhoods (unless employed to mow a white person's lawn). Young whites were conscripted to strafe neighbouring countries. Violent protests made black townships ungovernable.

The collapse of the Soviet Union prompted the African National Congress (ANC), the main black liberation movement, to abandon socialism. This made majority rule a less frightening prospect for white South Africans. After long negotiations, the apartheid regime allowed a proper democratic election in 1994, which the ANC easily won. The much-predicted civil war never happened, and now seems inconceivable.

The first decade of democracy has not been trouble-free. More South Africans now die each month from AIDS than were killed during the two decades of political violence before liberation. The fear of violent crime blights most South African lives. The murder rate is lower than a decade ago, largely because political killings have stopped, but South Africans are still five times more likely to be murdered than Americans are.

The government is popular, though, largely because of its efforts to improve life for those who suffered under apartheid. It has built 1.4m brick homes for the poor, and delivered free water, up to a modest limit, to 26m of South Africa's 45m people. The ANC has also established Africa's largest welfare state, most importantly through the provision of old-age pensions, which have transformed black grandmothers into the main breadwinners for many rural families.

All this was done without printing money. Fiscal discipline has been exemplary: the government's budget deficit has been reduced from 9.1% of GDP in 1993 to an estimated 2.4% in 2003. Economic growth, which averaged a miserable 0.6% a year between 1981 and 1993, ran at a more respectable 2.8% a year between 1994 and 2002, outstripping population growth of 1.8%. South Africa is much freer than ever before, and a bit more prosperous.

But that prosperity has not been evenly spread. The black middle class has grown bigger and wealthier; the government promotes blacks on principle, and private firms are obliged to do the same, under a raft of laws mandating “affirmative action”. According to Sampie Terreblanche, a left-wing academic, the richest 25% of blacks saw their incomes rise by 40% between 1974 and 1994 (as the worst apartheid restrictions on what they could do for a living were relaxed), and by a further 30% since 1994.

Poor blacks, however, have grown poorer. Mr Terreblanche calculates that the income of the bottom 45% of blacks halved between 1974 and 1994, and has contracted by another 10% since then. The main

reason is that unskilled South Africans are finding it harder to find work. Unemployment among blacks has increased from 24% in 1970 to 40% in 1994 and more than 50% today. That people should have lost their jobs during the turbulent latter years of apartheid is not surprising, because the country was getting poorer. But why, as South Africa has grown richer over the last decade, has it continued to shed jobs?

iAfrika

Liberation has brought prosperity for some...

Three factors seem important. First, under apartheid, blacks were deliberately deprived of education, leaving millions of them, as Mr Ncube puts it, unemployable. Second, the ANC has brought in new laws that make labour more expensive. Third, growth has not been nearly fast enough to make up for these structural problems.

There are two types of labour law. One sort is designed to improve working conditions, by mandating higher minimum wages, overtime rates, more maternity leave and so forth, and also makes it harder to sack anyone. This is marvellous for those who already have formal jobs, but it makes South African firms go into contortions to avoid hiring. The unskilled have lost out the most. “Look at that guy hawking oranges,” says James Lennox, head of the South African Chamber of Business. “If I was allowed to pay him what he would accept, I could create thousands of jobs.”

The other kind of labour law is designed to redress the wrongs of apartheid by compelling firms to promote more blacks, women and disabled people. Firms above a certain size are obliged to provide the government with annual reports outlining how they plan to make their workforce more “demographically representative” (ie 75% black, 50% female, etc) at all levels. Firms find this a hassle.

About half of South Africa's middle managers and a quarter of top managers are now black, up from hardly any a decade ago. Blacks have been promoted especially fast in the public sector. The government can pursue racial targets more easily, because it has no competitors and does not need to make a profit to survive. This makes the state less efficient. Since so many underqualified people have been promoted, the government has to hire an army of consultants to help them, who form what Ferial Haffajee, a local journalist, calls “a parallel bureaucracy”. Since, under “affirmative procurement” rules, black-owned firms can charge more and still win government contracts, fewer roads, bridges and houses for poor people are built than would have been without these rules.

...but not for others

Private companies compete fiercely for black talent. A black with sought-after skills is typically paid 15-20% more than a similarly qualified white, according to headhunters. Supply cannot match demand. There are many more blacks at university than ten years ago, but most choose soft subjects such as education and social sciences. In 2002, only 3,300 black high-school students (1% of the total) passed higher-grade maths. In the same year, only 246 of South Africa's 19,000 chartered accountants were black. Thabo Mbeki, South Africa's president, said he was disturbed, when he attended a graduation ceremony last year, to see that virtually all the students had specialised in “Biblical studies, Biblical studies, Biblical studies”.

Nonetheless, the government is convinced that many more blacks would have been promoted had racist white bosses not blocked their way. The director-general of the labour ministry, Rams Ramashia, threatened firms that failed to obey South Africa's new racial laws with being “fined to bankruptcy”.

The government is also trying to promote black share ownership. It has promised to issue a “black empowerment charter” for every industry, setting targets for the proportion of shares that must be transferred to blacks. Charters for the oil, mining and banking sectors have already been published. Details vary, but the general thrust is that about a quarter of South African shares should be in black hands within a decade or so.

Who will fund this colossal transfer of wealth? The total cost, according to Azar Jammine, chief economist at Econometrix, a consultancy, could be about 700 billion rand ($110 billion). That is equivalent to 10% of the country's money supply every year for ten years. Black South Africans do not have that kind money, nor could South African banks provide it without risk to their solvency. The government could foot the bill, but that would add ten points to inflation for a decade and lower the growth rate from 3-4% to 1-2%, estimates Mr Jammine, unless the assets somehow become more productive under their inexperienced new owners.

In practice, the cost will probably be split between the banks, the government, the firms divesting shares and the blacks buying them. Firms may win points for helping the government achieve its other objectives, by providing better training for blacks, for example. Some shares will go to funds with broad black ownership, but overall, the charters look like a hideously expensive way to enrich a small number of black people, many of whom will, on past form, be senior members of the ruling party. Empowerment, as currently practised, “has created no new products or independent new companies that are not propped up by large white corporations,” laments Moeletsi Mbeki, a prominent commentator and the president's brother.

Add value or fail

South Africa has a strong democratic culture, with a free press, an independent judiciary, a feisty trade-union movement and a large middle class. There are too many checks and balances for it ever to succumb to crude tyranny of the sort so common north of the Limpopo river. But the fact that the ANC faces no plausible electoral challenge is worrying.

South Africa's government is not particularly corrupt, but it could become so. If it remains in power for too long, the ANC could evolve into the kind of patronage machine that has so damaged virtually every other African country. Probably most of South Africa's black tycoons have links to the ANC. Cyril Ramaphosa, one of the richest, was the party's secretary-general, and the man who first promoted the idea of “empowerment charters”.

Looking further ahead, South Africa needs more genuine black entrepreneurs: people who build up their own businesses from scratch, rather than parlaying political connections into a chunk of a firm that someone else built; people who actually create wealth. Currently the whites pay most of the taxes, but their number is in long-term decline. Someone will have to take up the slack.

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Plenty of mistakes to learn from

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But if it can shake off the past, Africa might yet come round

A long, hard road ahead

HUMAN beings can learn from the past. Technological progress is cumulative, and information travels fast these days, which helps companies to produce more, better and cheaper goods each year. This is why most people in most countries grow a little richer each year. Surely, Africa cannot buck the trend forever?

One reason for pessimism, at least in the short term, is that many Africans, especially among the elite, seem to have drawn more grievances than lessons from history. It is natural and reasonable that Africans should resent the wrongs done to Africa during the colonial period, but resentment pays no wages. African politicians have a tendency to blame all ills on colonialism or its legacy, even in countries that have been free for decades. Many people believe in conspiracy theories: that western scientists created AIDS to kill Africans; that America was behind the war in Congo; that the IMF and the World Bank are, in the words of Namibia's president, Sam Nujoma, “the imperialists' well-organised machinery to get African cheap labour and raw materials for their economic development”.

Sometimes foreigners really are at fault. But rage at foreign wickedness should not become an excuse for inaction. George Ayittey, the Ghanaian writer, grumbles that: “Almost every black problem is explained in terms of a racialist paradigm, giving the false impression that black problems cannot be solved until racism is totally eradicated. [But] there will always be racism in the West. Must we blacks wait for its end before we take the initiative ourselves to solve our own problems?”

To be fair, African leaders do, from time to time, draw up plans to solve the continent's problems, but these plans tend to be over-ambitious and impractical. The African Union's current projects include a common currency (for countries whose inflation rates range from single digits in South Africa to triple, and perhaps soon quadruple, figures in Zimbabwe), and a common parliament. Less ambitious schemes would be more likely to succeed.

Hardly any of Africa's problems will be solved without sustained economic growth, but African leaders do not seem to be giving this the attention it deserves. In Japan in the 1960s, the government said that its top priority was to double national income within a decade. It took seven years. No African leader has pursued growth with anything like this degree of single-mindedness. Most seem keener on redistribution. South Africa's Thabo Mbeki said last year that even annual growth of 8% (more than double the current rate) would not help all the poor. But experience in other continents suggests that rapid growth improves even poor people's lives rapidly.

If Africa is to grow richer, it will have to produce goods and provide services that people wish to buy. Africa's leaders often demand that Africa's natural resources should be processed in Africa, allowing

Africans to capture more of the value added. Fair enough, but if they want to encourage such industries, they need to understand why it is that firms usually prefer to go elsewhere to cut and polish African diamonds, or refine African oil. Few do.

Straws in the wind

Despite its track record, Africa is not doomed. Some governments have shown that they can get some things right: think of Uganda's success in tackling AIDS, South Africa's peaceful transition from tyranny to democracy, or Botswana's tempestuous growth. The continent's wars have subsided, and AIDS may do so too. Most countries are moving towards greater democracy and a freer press.

Though governed by old men, Africa is a young continent. Half of its people are under 16, and more than 70% were born after independence. The “born-frees” are more inclined to blame their current rulers, rather than past colonists, for the state Africa is in. As they grow older and start voting, perhaps they will choose the pragmatic kind of leaders that Africa needs. Here's hoping.

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The future of computing

The next big thing?

Jan 15th 2004 | SAN FRANCISCO
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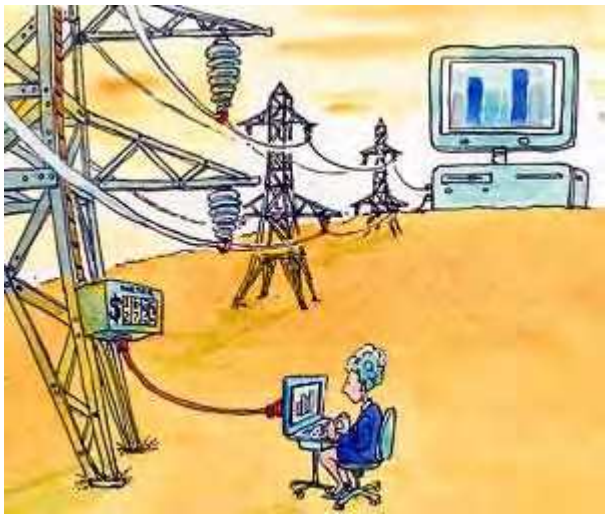

The uncertain promise of computing that is foolproof, invisible and everywhere

IT IS increasingly painful to watch Carly Fiorina, the boss of Hewlett-Packard (HP), as she tries to explain to yet another conference audience what her new grand vision of “adaptive” information technology is about. It has something to do with “Darwinian reference architectures”, she suggests, and also with “modularising” and “integrating”, as well as with lots of “enabling” and “processes”. IBM, HP's arch rival, is trying even harder, with a marketing splurge for what it calls “on-demand computing”. Microsoft's Bill Gates talks of “seamless computing”. Other vendors prefer “ubiquitous”, “autonomous” or “utility” computing. Forrester Research, a consultancy, likes “organic”. Gartner, a rival, opts for “real-time”.

Clearly, something monumental must be going on in the world of computing for these technology titans simultaneously to discover something that is so profound and yet so hard to name. What is certainly monumental, reckons Pip Coburn, an analyst at UBS, is the hype, which concerns, he says, “stuff that doesn't work yet”. Frank Gens at IDC, another tech consultancy, quips that, in 2004 at least, “utility” computing is actually “futility” computing.

Yet as a long-term vision for computing, what the likes of IBM, Microsoft and HP (and Oracle, Sun, etc) are peddling is plausible. The question is, how long will it take? Some day, firms will indeed stop maintaining huge, complex and expensive computer systems that often sit idle and cannot communicate with the computers of suppliers and customers. Instead, they will outsource their computing to specialists (IBM, HP, etc) and pay for it as they use it, just as they now pay for their electricity, gas and water. As with such traditional utilities, the complexity of the supply-systems will be entirely hidden from users.

ER meets the Matrix

The potential for a computing infrastructure such as this to boost efficiency—and even to save lives—is impressive. Irving Wladawsky-Berger, an in-house guru at IBM, pictures an ambulance delivering an unconscious patient to a random hospital. The doctors go online and get the patient's data (medical history, drug allergies, etc), which happens to be stored on the computer of a clinic on the other side of the world. They upload their scans of the patient on to the network and crunch the data with the processing power of thousands of remote computers—not just the little machine which is all that the

hospital itself can nowadays afford.

For its nuts and bolts, this vision relies on two unglamorous technologies. The first is “web services”—software that resides in a big shared “server” computer and can be found and used by applications on other servers, even ones far away and belonging to different organisations. Mr Wladawsky-Berger's hospital would be getting the patient's info from his home clinic through such a web service.

The second technology is “grid computing”. This involves the sharing of processing power. The best-known example is a “search for extra-terrestrial intelligence” project called SETI@home, overseen by the University of California at Berkeley. Nearly 5m people in 226 countries have downloaded a screensaver that makes their computer available, whenever it is sitting idle, to process radio signals gathered from outer space. The aim is to find a pattern that may be from aliens. Mr Wladawsky-Berger's hospital would similarly crunch patient-data using the internet, or grid, as if it were a single, giant virtual microprocessor, but for a more earth-bound purpose.

Both technologies have made great strides recently. Web services, for instance, need common standards and protocols. Some basic standards already exist—awkward acronyms such as XML, SOAP and WSDL provide a rudimentary grammar to let computers talk to each other. But the sticking point, says Phillip Merrick, boss of webMethods, one of the pioneers in the field, has been the many other fiddly but necessary protocols for security, transaction certification, and so on. A breakthrough occurred in October, when the two superpowers, IBM and Microsoft, simply got up on a stage together and declared what protocols they will use. Dubbed “WS splat” by the geeks, this ought to speed up the adoption of web services.

Web services are currently most visible in the business model of so-called application service providers. These are firms that offer to host software applications and databases for customers for a monthly fee—an analogy would be for firms to do their e-mailing via Yahoo! or their buying via eBay. The most successful is Salesforce.com, a San Francisco firm that, as the name says, specialises in software for managing customer information and marketing leads. It says that it was poaching so much business from a more traditional seller of customer-relations software, Siebel Systems, that Siebel had to adopt the model itself. In October, Siebel teamed up with IBM and now also offers its software as a service over the internet.

Nonetheless, this particular form of web services is overhyped, says Rahul Sood of Tech Strategy Partners, a consultancy in Silicon Valley. Such services appeal mostly to small businesses and firms that do not need to customise their applications very much. For the grander vision—the on-demand, adaptive, seamless, ubiquitous, organic sort—a lot more needs to happen.

At the core of the vision is flexibility—a firm must be able to make its operating costs, and therefore its computing and information costs, totally variable so that they go up and down with business volumes. Firms can improve cost flexibility today, says Mr Sood, but only if they stick with one vendor, such as IBM, or if they make only one of their many computing functions (data storage, say) flexible. But for computing to be bought and sold as a utility, firms must be able to switch vendors, to do it for all their computing functions, and with meter-based pricing. All of this will take a few more years to get right.

And yet, though some years away, the very idea of utility-style computing is making waves today. IBM already describes practically every major corporate sale, whether of humdrum servers or of comprehensive consulting, as having to do with its “on demand” vision. This is forcing HP, its arch rival, to redouble its efforts to be seen less as a box-shifter and more as a provider of “solutions”. And software suppliers are preparing for a different revenue model: instead of chunks of licence fees at point-of-sale, monthly-usage fees will trickle in from their customers.

Still, it is tempting to conclude that the current marketing hype of the big computer firms is meant mostly to obscure the humdrum reality that overall tech spending will not regain the fizz of the bubble era any time soon. Instead, the new model of computing, says Halsey Minor, founder of Grand Central Communications, one of the many firms that are now working out the details of web services, is inevitable and important, but “sooo boring”.

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Nanotechnology

The next small thing

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A bright little idea comes to market

THINK about the difference between cement and sea-shells, and nanotechnology begins to make sense. They are made of roughly the same chemical elements, but the atoms are arranged differently. In short, they have different nanostructures, which is why cement crumbles when cut thin, but delicate shells endure. Nanotech's appeal is that it offers the potential to control nanostructures.

When George Bush signed the National Nanotechnology Initiative into law last month, he boosted America's investment in a nascent technology that has been hyped for years. There is talk of a market value of $2 trillion by 2015, from perhaps as little as $1 billion today.

Is nanotech an industry, a process, or something else? David Bishop of the New Jersey Nanotechnology Consortium defines it broadly as “devices, structures or systems with characteristics, features or parts on a nanoscale”—that is, less than one billionth of a metre.

In America, corporate giants such as General Electric, Motorola, DuPont and Lucent are now pursuing nanotech. Boeing is working on applications to cut the weight of rockets, aircraft and satellites. Kodak has focused on uses in flat-screen displays, inkjet paper and medical imaging. 3M sees potential applications in optical films, self-cleaning glass and dentistry.

Thus far, large firms are mostly drawing on outside research, much as big drug firms buy in biotech, says Sean Murdock of AtomWorks, a nanotech research and development organisation. That helps to explain the boom in nanotech start-ups. McKinsey, a consultancy, counted 837 nanotech start-ups in 2003—over half in America—up from 462 in 2001.

Nanotech still faces big challenges in the journey from lab to widespread commercial use. Manufacturing processes must become cheaper. Social and environmental concerns may have to be addressed. Private investors have so far been cautious, because likely winners are hard to identify. Much of the funding so far is by government—rising, according to McKinsey, from $825m worldwide in 2000 to $3 billion in 2003.

Already on the market are sunscreens that do not leave a white zinc residue and sports shirts that are unusually waterproof and stain-resistant. Next in line are nanoproducts in chemicals, coatings, sensors and cosmetics. Beyond that, new products are expected to follow in lighting, medical diagnosis, drug delivery and computing. This week, Intel, the world's biggest chip-maker, announced a collaboration with Nanosys, a start-up based in Palo Alto.

In America, the north-east, northern California and Chicago are emerging as nanotech hubs. “You need to be close to the clusters of innovation to get people who've interacted with leaders in the field,” says Cedric Loiret-Bernal of NanoInk, a Chicago-based start-up.

A key challenge for firms and investors is where to focus. “Fortunes are going to be made and lost,” says Mr Bishop. “That's the beauty of capitalism. It will reward those who guessed right and punch those who didn't.” The products may be tiny, but the stakes are enormous.

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White-collar crime

Flipping hell

Jan 15th 2004 | NEW YORK
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Some sympathy for the criminals?

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The flipping Fastows

ANYONE who has followed the obtuse, uncertain meanderings of prosecutors in the trial of Tyco's ex-boss, Dennis Kozlowski, will understand why the government prefers its white-collar criminals to plead guilty rather than face trial. Yet, hard as it can be to win a conviction in court for white-collar fraud, other methods of securing justice are not without controversy. This week, as Enron's former finance chief, Andrew Fastow, and his wife, Lea, struck a plea bargain with prosecutors that will see Mr Fastow get a ten-year sentence, there were stirrings of sympathy for the couple.

Although the government earlier bagged a few bit players in the Enron tragedy, prosecutors have struggled to nail the firm's former top executives. Prosecutors often strike plea bargains in exchange for evidence against higher-ups, a technique known as “flipping”. So Mr Fastow's cooperation may spell trouble for his former bosses, Kenneth Lay and Jeffrey Skilling.

Having at first declined to co-operate, Mr Fastow's resolve weakened with the indictment of his wife last May. Recent negotiations indicate that the couple, who have two small children, had been trying to ensure that Lea finished her sentence before her husband started his. At the time of her indictment, Mrs Fastow's lawyers claimed she was being charged so as to put pressure on her husband to cooperate, and accused the government of “unfair and unjust” practices. Although Mrs Fastow filed false tax statements and created and administered an off-balance-sheet special-purpose entity that Enron used to hide its control of some Californian wind farms, some reports have claimed she was an innocent who fell under the malevolent influence of her husband. Sherron Watkins, the celebrated Enron whistleblower, told *Business Week* that Mrs Fastow was “plump and sweet”. Elsewhere in scandal-land, Sam Waksal pleaded guilty to charges of insider trading in the shares of his firm, ImClone, in return for keeping his daughter out of jail. He is serving a seven-year sentence.

Perhaps prosecutors are right to use the same hardball tactics in white-collar cases as they do, say, to prosecute mafia families. As US attorney for the southern district of Manhattan, James Comey brought most of the big fraud cases now filling the courts. Mr Comey liked to point out that he treated suspects in white-collar cases just like everyone else—though he did admit making special arrangements for Scott Sullivan, WorldCom's former finance chief, who asked that his daughter be shielded from his “perp walk” in handcuffs. Mr Comey's attitude has done him no harm: he is now America's deputy attorney-general.

If the fate of the Fastows and Mr Waksal fails to soften hearts, consider the unfortunate rich people who the Internal Revenue Service (IRS) is pursuing for their use of “abusive” tax shelters in the 1990s. Wary of being entangled in the sort of lawsuits that dogged earlier moves to stamp out shelters, the IRS has persuaded Congress, in the case of one shelter called BLIPS, to rewrite the law to make BLIPS-like vehicles illegal—and then to go one step further and make the new law retroactive. This week, the geniuses at KPMG who cooked up BLIPS and other such schemes finally lost the will to fight with the government, and ousted their deputy chairman, Jeffrey Stein. Perhaps Mr Kozlowski's prosecutors, increasingly at risk of defeat, now need a similar device—a retroactive law to make, say, buying dog-umbrella stands and throwing toga parties a capital offence.

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Oil

Shell shock

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A dramatic cut in Shell's reserves has the oil world buzzing

HOW on earth can an oil company lose a fifth of its reserves overnight? And not any old oil company, but that very model of a modern oil major, Royal Dutch/Shell, which has long boasted of the excellence of its management.

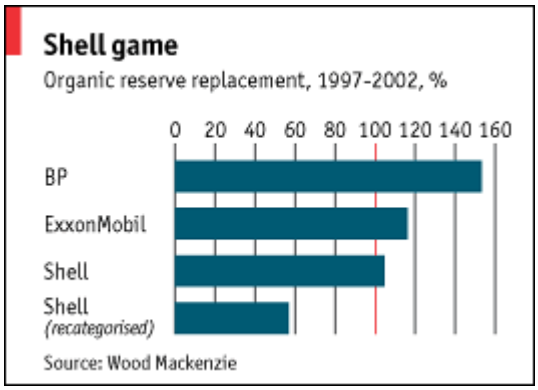
On January 9th, Shell said that it was downgrading nearly four billion barrels of oil and gas—a whopping fifth of its total reserves—from "proven" reserves to "probable" or other, even less-certain, categories. As proven reserves are one of the main metrics used by analysts to value oil firms, investors were not pleased. Shares in the world's third-biggest oil firm promptly fell by 7%, amid fears of worse to come.

In some respects, Shell's shock news is not as bad as it seems. The firm has not actually lost any oil. Michael Lynch of Strategic Energy & Economic Research, an industry consultancy, explains that, under the oil industry's murky accounting practices, "shifting a project from proven to probable is like moving it out of a cash account to accounts receivable. It is still an asset, but not as valuable because of the lower certainty." Shell still expects to bring most of the reclassified oil and gas to market eventually. It stresses that there has been no restatement of financial results, like at Enron or WorldCom—though it is surely undeniable that the firm has restated data of great importance to investors.

Still, this fiasco could yet lead to big changes, both at Shell and in the industry as a whole. The firm's boss, Sir Philip Watts, was never a favourite of investors, but now he faces intense pressure to go. He has long been seen as aloof and uncommunicative—an impression he reinforced this week by going to ground and leaving other executives to manage the bad news.

Now investors are questioning his competence. The revised figures suggest that, on Sir Philip's watch, Shell has performed far worse than previously thought on several important measures. Wood Mackenzie, a consultancy, calculates that in 1997-2002, the firm's rate of replacement of reserves—which are inevitably depleted as firms pump hydrocarbons out of the ground—was not 105% as previously thought, but an abysmal 57%, significantly below that of both BP and Exxon Mobil (see chart). Recalculated, Shell's "finding and development" costs in that period jump from an already relatively high $4.27 per barrel to $7.90 per barrel.

There is no evidence of criminal wrongdoing. And there is no precise legal standard or industry agreement on how to classify reserves. Under guidelines on what firms can call "proven reserves" issued by America's Securities and Exchange Commission (SEC), managerial discretion is allowed and reclassifications tolerated. Indeed, revisions—both up and down—are fairly common. What is uncommon is the breathtaking size of this reduction in reserves, the largest ever.



As has been widely noted, Sir Philip was previously in charge of Shell's exploration and production. That means that he knew, or should have known, how accurately the firm was booking new oil and gas discoveries. All eyes will be on him at Shell's fourth-quarter results presentation, due on February 5th—if he is there.

Shell's error may prompt an industry-wide move towards standardisation, and perhaps firmer regulation, of the booking of reserves, even though Shell's rivals are standing by their own numbers. Chevron Texaco and Exxon Mobil, for example, are Shell's partners in Australia's giant Gorgon gas project, which

accounted for a big part of Shell's recent reclassification. But, unlike Shell, both firms say that they did not book Gorgon's reserves as proven.

The rewriting of Shell's history is so dramatic that the SEC is likely to investigate. It already has a small enquiry under way, triggered by questions about how firms were booking reserves in the deep waters of America's Gulf of Mexico.

Investors, too, may demand greater transparency. After all, if they can't be sure of trusty old Shell, how can they believe smaller, perhaps shadier, operators?

The most ironic suggestion now making the rounds is that the world's biggest oil companies should permit independent verification of reserves by outside consultants. Russian oil firms, with a well-deserved reputation for dodgy dealings, were forced to adopt that sensible if ego-deflating measure in order to satisfy the demands of western investors. How embarrassing it will be if the industry's proudest names are now put to the same test of transparency.

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Gold mining

Mr Jonah goes to Jo'burg

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From The Economist print edition

A giant digs deeper for African gold

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SEEN from the perfect lawn beside the white colonial-era walls of Sam Jonah's house in Obuasi, Ghana, gold mining seems to be an unchanging and tranquil business. For over a century Ashanti Goldfields has dug gold from deep in the valley below. This hill-top perch, ringed with palms, is a quiet retreat for the man in charge. But later this year, Mr Jonah moves south to the skyscrapers and noisy streets of Johannesburg, to serve as president of South Africa's AngloGold. He will work under AngloGold's boss, Bobby Godsell, who struck a deal last year to buy Ashanti for $1.4 billion in shares.

By May, the euphemistically titled “merger”—the gigantic AngloGold, in fact, is swallowing Ashanti—will be completed to form arguably the world's biggest gold miner. With annual production of more than 7m ounces, a market capitalisation of about $11 billion, and probable and proven reserves of 93m ounces, it should outgun all rivals. The combined group expects to earn profits of $1 billion a year, before interest and tax. As the man responsible for the public face of the expanded firm, as well as for overseeing its new expansion in Africa, a lot more is likely to be heard of the charismatic Mr Jonah.

Ashanti needed an outsider with deep pockets to keep it digging. AngloGold promises to invest $220m, plus $44m over five years for deep exploration, just for the centrepiece mine, Obuasi Deep. After years of under-investment it will swallow money—quite likely, more than AngloGold has bargained for. Machinery has been endlessly patched up, rows of ramshackle trucks line the workshops, and environmental blunders have denuded nearby hills that must be replanted. Miners in narrow, gloomy tunnels swelter due to the poor ventilation.

The cost of reaching large and high-grade deposits 5,000 feet (1,500 metres) below the surface, in order to extend the mine's life by perhaps 40 years, could easily top $500m. Plans to develop some other assets depend on political stability coming to the Democratic Republic of Congo and Zimbabwe. Joint operations, especially at Geita mine in Tanzania, could save perhaps $15m a year, but that is tiny given the demands at Obuasi.

It is, though, bearable for cash-rich AngloGold—at least while the gold price is buoyant. It recently touched $430 an ounce, a 15-year high, and it may rise more against a weak dollar. Gold tycoons should be in clover, but both Mr Godsell and Mr Jonah have seen the price flip-flop between $800 and $250 in the past two decades. Such swings can destroy an ill-managed firm, as nearly happened at Ashanti in 1999 when Mr Jonah's plan to hedge against a low gold price went disastrously wrong.

That blunder almost bankrupted Ashanti, scared off creditors and ultimately forced Mr Jonah into the arms of his South African buyers. He sums it up coyly: “consolidation is a logical reaction to a very volatile market”. Now AngloGold will hedge for the combined firm. Though it has a much better reputation for hedging, it will struggle to cope with the high costs of its large South African mines and the strong rand, which has cut profits and forced many South African miners to shed jobs and talk of closing shafts.

A risk remains in Ghana, where politicians must be placated. Last month, opposition parliamentarians objected to AngloGold as a meddling foreign firm. Though the government backs the sale—both as a shareholder and industry regulator—it wants promises of long-term job protection. To minimise future political interference, AngloGold has struck a “stability agreement” to guarantee corporate-tax and royalty rates for the next 15 years.

But there might be another way to ensure good relations with Ghana's authorities. If Mr Jonah finds the hurly burly of Johannesburg trying, he could always return to the country where he has long been tipped as a future president. That charming villa in Obuasi would then be in striking distance again.

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Privatisation

The Lithuanian way

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A botch-job in the Baltics

FOR a small country, Lithuania has had some big problems privatising state-owned industries left over from Soviet days. The sale of the biggest of them, the Mazeikiai oil refinery in 1999—to an American firm which quietly moved it on to a Russian one—caused so much fuss that the then prime minister, Rolandas Paksas (pictured), resigned in protest and then exploited public anger at the deal to win an upset victory in a presidential election three years later.

Lithuania's recent sales of two state-owned alcohol firms have been similarly colourful, if on a smaller scale. One of the deals collapsed in October when the supposed buyer, an Italian, failed to turn up at the signing ceremony. The other provoked a flurry of protest when the top bidder, a firm from neighbouring Latvia, was rejected in favour of an underbidder from Lithuania. A parliamentary inquiry has since found that the local firm got leaks of confidential information about the deal from Mr Paksas's office. That charge forms part of the impeachment proceedings which the parliament launched against the president in December.

AFP

Would you buy a used firm from this man?

Now the Lithuanian government may be about to botch another deal. Last autumn, it put the country's electricity-distribution industry up for sale, in the form of two firms, one serving the west of the country, the other the east. The sale of the western firm was aimed at domestic investors, and went smoothly. Not so the sale of RST, serving the eastern half of the country, which was offered to foreign investors.

RST has attracted a serious bidder at a serious price—about €150m ($190m). The trouble is, the bidder comes from Estonia, Lithuania's even smaller near-neighbour in the Baltics. Regional rivalry runs deep, and selling out to uppity Estonians may be more than Lithuanian pride can bear.

Lithuania wanted a buyer from western Europe. But its best hope, a German company, E.ON, dropped out at the last minute, leaving Estonia's Eesti Energia as the only contender. Eesti Energia's offer is valid until March, but a Lithuanian parliamentary committee has already advised postponing the sale of RST for a year or two, and the embarrassed government seems sorely tempted to agree.

To explain its reluctance, Lithuania claims that Eesti Energia is too small and too indebted to inspire confidence as an owner. It is also a state monopoly that, says Lithuania, will have to be restructured and probably privatised in its turn, making the final ownership of RST uncertain.

These arguments ring hollow. Though a tiddler by world standards, Eesti Energia is five times the size of RST in profits and assets. Its credit rating is higher than Lithuania's own sovereign rating. It has been restructured already into separate accounting and operating units, meeting European Union rules in preparation for Estonia's EU entry in May. It may be privatised sooner or later, but probably through a public offering rather than a trade sale.

Besides, says Eesti Energia, the Baltic countries have similar strategic interests. They all fear dependence on Russia. If Lithuania is worried about an eventual Russian takeover of its power industry, then that is a worry which Estonia shares at least as strongly.

Eesti Energia is pushing for regional consolidation. Three years ago it sought a merger with Latvia's state

power-monopoly, Latvenergo, but was blocked by political opposition. If it cannot get RST, it is likely to turn its attentions back towards Latvia. And it can hope to get its way in Lithuania after EU enlargement in May, when companies from all EU countries will have to be treated equally.

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Viral marketing

Drink to that

Jan 15th 2004 | WELLINGTON, NEW ZEALAND
From The Economist print edition

Politically incorrect can work wonders

FOR small firms with limited budgets but big ideas, the internet continues to be a marvellous way to get known—especially when it is married to one of adland's oldest ploys: creating a bit of controversy. Even better if it also raises a laugh. One of the latest firms to pull off this trick, using online “viral marketing”, is 42 Below, a New Zealand producer of premium spirits.

Last month, New Zealand's Advertising Standards Complaints Board deemed that the most recent in a series of politically incorrect advertisements run by the company was in such poor taste that the independent distiller agreed to (temporarily) remove it from its website. Now, of course, there is a clamour to hear the ad. It depicts Maoris, New Zealand's indigenous people, drinking “large amounts of 42 Below” and “exchanging it with the white man for muskets, blankets and Hobbits.”

“It's always the way with cutting-edge humour,” says 42 Below's founder, Geoff Ross, who started the three-year-old company as a hobby while working for Saatchi & Saatchi, a giant ad agency. He plans to restore the ad to the company's website within days to meet demand from people desperate to hear it.

Mr Ross says his ads have helped lift sales of his vodkas from 500 cases in December 2002 to 3,500 cases last month. No doubt they also helped with the firm's recent initial public offering, which was oversubscribed. 42 Below is now expanding into America, and introducing a gin called South.

“Even if we had the resources to blitz New York or Los Angeles, that wouldn't be the right approach because the people we want to reach reject mass marketing,” adds Mr Ross. Viral marketing relies on the message spreading around cyberspace, often by one person sending to a friend a website link of something they find interesting.

It is important to be subversive, he adds, and to be willing “to take the piss out of yourself.” His online ads not only dare to make light of Maori alcoholism, but also gay stereotypes, the All Blacks rugby team, America's Cup sailing and misconceptions which Kiwis face when travelling abroad. In a new ad, a supposed immigrant employee testifies that working for 42 Below beats making sneakers in a sweatshop in China, because he gets all the rice he can eat, “and they lock us in at night, for our own safety.” It pushes the limit. But as a former adman, Mr Ross knows that when marketing goes unnoticed, it fails.

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About sponsorship

Face value

The Boeing-beater

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From The Economist print edition

AFP

Can Noël Forgeard keep Airbus flying high?

PHIL CONDIT was forced to quit as boss of Boeing in November. Meanwhile, his counterpart since 1998 at Airbus, Noël Forgeard, goes from strength to strength. True, profits at Airbus were flat last year, and may dip this year as deliveries of new aircraft slip below 300. The firm is spending heavily on the launch of the new Airbus A380 super-jumbo. Yet Mr Forgeard crows that he finished the year with a cash pile that had grown by hundreds of millions of euros. He thinks Airbus is perfectly positioned to benefit from what he expects to be a steady revival of travel, which will lead airlines to order more planes in the second half of this year.

Despite all the recent travails of the airline industry, that may not be an unrealistic hope. Last week British Airways (BA) reported its first growth in “premium traffic”—highly profitable business travellers—in three years. That was a thoroughly welcome announcement, coming as BA suffered delays and cancellations due to security fears about some of its flights. Air France, KLM and Lufthansa also announced stronger traffic recently. In the past year airline shares have nearly doubled on hopes that big carriers in America and Europe are about to recover financially. Shares of EADS (European Aeronautics, Defence and Space, the parent of Mr Forgeard's Airbus) have also nearly doubled in the past year, even while scandal-ridden Boeing has struggled.

Mr Forgeard took command of Airbus two years before it became a genuinely integrated company. Then, it was merely a consortium for product development and sales, with planes manufactured by a consortium of Aerospatiale, Dasa (part of DaimlerChrysler), British Aerospace and Spain's Casa.

Even with that loose structure, Airbus won 40% of the world market, under the controversial, ebullient leadership of Jean Pierson. Mr Forgeard, who came from France's Lagardère defence business, is quieter and more disciplined. Under his leadership, Airbus has focused on profit, while continuing to squeeze Boeing's market share. The rather traditional engineers at Airbus's base in Toulouse, more accustomed to spending than controlling costs, have come to respect his stress on the bottom line. He has used his new clout as boss of an integrated firm to slash costs and raise productivity by around 5% a year.

Boeing, too, has slashed costs, but has been forced to do so by plunging sales. The jumbo American firm has cut some 40,000 jobs from its commercial-airliner business, and barely remained profitable as orders dried up and its output fell by half. Airbus, by contrast, merely cancelled plans to ramp up production, and has managed to maintain profit margins at a healthy 7%.

In 2003, Airbus beat its American rival on orders for the fourth time in five years. As well as better marketing and efficiency gains, Mr Forgeard has also delivered better products—and called market trends more accurately.

Airbus's single-aisle planes offer a more comfortable cabin than Boeing's older 737s, and some of the later versions of its wide-bodied A300-A340 family are proving formidable competitors to Boeing's 777. Airbus delivered more planes than Boeing in 2003, 300 compared with 285, and is likely to do so again this year. In the past two years, it has broken into the low-cost airline market, loosening Boeing's grip on this fast-growing segment by winning big orders from easyJet in Europe and JetBlue in America. Most analysts expect it to dominate for the next five years.

Despite the fast-waning attractions of Boeing's ageing staple products, it has struggled to invent new aircraft that appeal to its customers. Two years ago, it unveiled plans for a sexy new near-supersonic aircraft—soon after its failure to sell a proposed new version of its venerable 747 jumbo. This could have forced Mr Forgeard into panic measures—but he confidently predicted that Boeing would not find enough buyers to launch the plane, and would be forced instead to use the same technology to make a plane that would be 20% cheaper to operate than existing planes of this size. In due course, Boeing shelved the Sonic Cruiser in December 2002, and is now trying to launch a 250-seater called the 7E7. So far there are no takers, not even in Japan, where Boeing is traditionally strong. Mr Forgeard is convinced that Boeing will go ahead, but that, if it brings a plane into production as planned in 2008, its technology will not be good enough to outperform existing Airbus A330s. His (self-serving) advice to Boeing is to wait a while for a leap in technology. Having correctly judged the mood of the market, it is no surprise that Mr Forgeard's newest offering, the 555-seater A380, has already won 129 orders—halfway to the break-even point.

Clouds on the horizon

Even so, there are problems ahead for Mr Forgeard. As fast as he cuts costs at Airbus, the fall in the dollar eats away at profits. Airliners are priced in dollars, whereas at least half of Airbus's costs are in euros or the equally strong British pound. Even hedging and purchasing more parts from America will not make that problem go away entirely. Mr Forgeard's dream of pricing planes in euros is unlikely to make much headway.

Nor has the A380 yet won a single order in Japan, whose airlines are the biggest users of today's big jets—and Mr Forgeard does not expect any until 2005. The worry for Airbus is that Japanese carriers, once they are in a financial position to upgrade their fleets, will stick with Boeing. Already Boeing has signed up Japanese manufacturers as partners on the 7E7 programme. Mr Forgeard wants the European Commission to oppose Japanese government aid that is going into Boeing's project, arguing that this breaks World Trade Organisation rules on such subsidies. Lastly, Airbus must also contend with the unquantifiable risk of another successful terrorist act—a risk about which, alas, Mr Forgeard, like most people, can probably do nothing.

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Europe's corporate governance

Parma splat

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What are the lessons from the scandal at Europe's largest dairy-products group?

WHEN the Parmalat scandal first began to unfold in December, it was easy to jump to the conclusion that the collapse of this huge publicly-quoted group, still 51%-owned by the Parma-based family of its founder Calisto Tanzi, exemplified little more than the dark side of Italian business. But as more and more details of the company's disappearing billions have come to light, it is clear that this is no uniquely Italian affair.

At the heart of the scandal lies a letter, purportedly from the Bank of America—founded a century ago this year (with no little irony) as the Bank of Italy—in which the bank confirmed that Bonlat, a Parmalat subsidiary based in the Cayman Islands, had deposits of close to €4 billion ($5.5 billion) with the bank. Fausto Tonna, Parmalat's former chief financial officer and one of ten people (including his wife) who are currently under arrest over the affair, has told prosecutors that he benefited personally from funds held by subsidiaries in Luxembourg, and he has alleged that the company took kickbacks from the Swedish packaging group Tetra-Pak—an allegation that the Swedish company has denied. The splat from Parmalat is spreading far and wide.

As in the comparable scandal at Enron, the attention of investigators has been sharply focused on the auditors. Until 1999, Grant Thornton, an international network of accounting firms, was Parmalat's main auditor. But Italy's rules on the mandatory rotation of auditing firms at regular intervals forced the group to switch that year to Deloitte & Touche, one of the big four global accounting firms.

Rotation of auditors—one of the more controversial measures introduced in July 2002 by the Sarbanes-Oxley act, America's response to Enron, WorldCom and other corporate scandals—seems to have been of little use here. Grant Thornton continued as the auditor of Bonlat and relied on the Bank of America letter for evidence of the Parmalat subsidiary's assets until, in mid-December 2003, Bank of America said that the document had been forged: the cash simply did not exist. Without the money, Parmalat's empire came crashing down. It is now operating under a new bankruptcy law—protected from immediate liquidation by its creditors—which was rushed through Italy's parliament at the end of last year.

Last week, Grant Thornton expelled its Italian member from the network. “We do not tolerate behaviour that deviates from our ethical standards,” it said, mindful no doubt of the fate of Arthur Andersen, the auditing firm which was forced to disband after the disclosure of its role in the scandals at its erstwhile client, Enron. But how could Grant Thornton's Italian arm have failed to detect the forgery? Standard practice is for auditors to write independently to banks for confirmation of cash balances. Grant Thornton,

it seems, relied on Parmalat's internal mail to deliver its letters seeking confirmation, an astonishing lapse that allowed the fraud to continue. Several of the firm's employees are now under investigation, and on January 8th magistrates called in the first Deloitte partners to explain their firm's role in the affair.

Transatlantic similarities

The parallels with America's corporate scandals do not end with the fallibility of auditors. The lack of independence of non-executive directors on the board is another issue in common. Parmalat's was stuffed with family members and local cronies. Despite a 1999 reform that imposed independent directors on listed Italian companies, big ones such as Parmalat were allowed to opt out.

Moreover, Mr Tanzi was both chairman and chief executive of the group, now acknowledged in America and Britain as a potentially dangerous combination. There also seems to have been close complicity between him and the chief financial officer, with Mr Tanzi and Mr Tonna echoing the roles of Jeff Skilling and Andrew Fastow at Enron, of Bernie Ebbers and Scott Sullivan at WorldCom, and of Dennis Kozlowski and Mark Swartz at Tyco. And everywhere there were employees who either knew or suspected what was going on but who, for one reason or another, were dissuaded from blowing the whistle.

The Parmalat case may seem to differ in the simplicity of its fraud. The audited statements from Bonlat were used to show cash balances that were reported by the parent company as offsetting high levels of debt on its balance sheet. Each quarter a set of forged documents would show purported cash holdings at Bonlat that matched the head office's requirements. Deloitte seems to have accepted Grant Thornton's audits unquestioningly, while bankers and investors took the audited group figures as reassurance that, although complex, the group's finances were essentially sound. They failed to ask why a company with so much cash needed to borrow so much.

The deceit continued for several years and might have originated as an effort to cover up losses at the group's Brazilian operation (said to be considerable), or to conceal the Tanzi family's siphoning off of cash, or to retrieve complicated financial derivatives deals that went badly wrong. Whatever the case, and it may have been a combination of several things, matters clearly got wildly out of control.

But the fraud may have been more sophisticated than it might at first appear. “What is the one line in an audited balance sheet that no one questions?” asks a former auditor with Deloitte &Touche. “Answer: the cash and other short-term assets line. And that is precisely where this fraud was directed.” Moreover, it was not sufficient for Bonlat and other group entities merely to claim fictitious cash balances. They also had to generate a paper trail of false sales to show where the money was supposedly coming from.

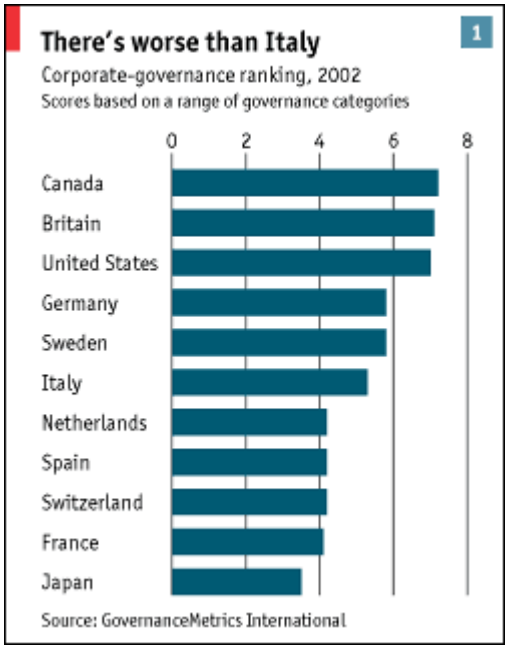
Embedded deception

“None of this has a specifically Italian flavour,” argues Christopher Seidenfaden of Unicredit Banca Mobiliare, an Italian bank. “We're talking about a fraud that could have happened anywhere.” Umberto Mosetti, a law professor attached to Deminor, a consultancy that specialises in corporate governance and shareholder rights, says that the main legal issues in the Parmalat case are false accounting, insufficient disclosure and the provision of misleading information to investors.

Largely through takeovers, Parmalat had become an international business, and it was clever at exploiting the different standards of financial markets. Lawsuits have already started to fly in America, where the company sold more than $1.5 billion-worth of bonds to American investors, including several big life-insurance companies. While there are specific local Italian rules and laws that were broken by Parmalat and/or its auditors, the fraud went way beyond them.

“It fooled a lot of people that Parmalat was able to maintain a New York listing for its American Depository Receipts (ADRs),” notes Mr Seidenfaden. Investors were reassured that Parmalat was satisfying American regulatory requirements. They were also reassured by the repeated willingness of the biggest international banks to underwrite new bond issues for the company. Citigroup and Deutsche Bank—respectively America's and Germany's leading banks—both underwrote Parmalat bonds, as did Bank of America.

Once Parmalat had gathered its audited numbers, however, it was almost impossible for external parties to crack the fraud. Mr Tanzi fought a long-running legal battle with Lehman Brothers, an investment bank which he accused of rigging the markets in order to damage Parmalat. Credit-rating agencies asked plenty of questions, but they were unable to see past the deception. Regulators from Milan to New York were also hoodwinked and there was no way they could reasonably throw out Parmalat's filings.



Giulio Tremonti, Italy's finance minister, has suggested that more effective local regulation might have prevented the fraud. He has proposed a law that would change the regulatory responsibilities of the country's different agencies. The idea of tougher regulation for Italy's financial markets is fine, but there are suspicions that Mr Tremonti is playing politics.

By trying to shift responsibilities, he is explicitly attacking the powers of the Bank of Italy, which oversees all banking activities—including the issuing of bonds. Under Antonio Fazio, its governor, the central bank has been stoutly independent, often acting against the government's wishes. “The real danger is that poor legislation will be rushed through,” says Mr Mosetti. “Then we could be worse off.”

Rogue states

Italy has a reputation for poor corporate governance combined with the shameless exploitation of minority shareholders. But much the same can be said of other European countries, including France, the Netherlands and Switzerland, where this week Adecco, the world's largest temporary-employment agency, said it expects to delay the announcement of its 2003 results because of “possible accounting, control and compliance issues...in certain countries”. Most European countries have mere codes of practice for corporate governance, rather than legal statutes, and progress towards meeting the standards of the codes has been patchy at best.

In Germany, a government-appointed commission led by Gerhard Cromme, a former chief executive of ThyssenKrupp, a steelmaker, published recommendations for the reform of corporate governance, a so-called “Kodex” of best practice, in February 2002. With this, Germany's first governance code ever, the government was hoping to boost foreign investment.

But the majority of the Cromme recommendations are voluntary, though firms that do not comply have to explain to shareholders why. So far, most German companies have introduced uncontentious measures in the Kodex, such as improving communication between the supervisory board and shareholders. Many of them have set up a separate audit committee, as also suggested by the Kodex, and some have strengthened the independence of their supervisory boards by, for instance, limiting to two the number of board seats available to former members of the company's management.

Nevertheless, they have largely ignored the bits of the Kodex that they do not like. For example, the implementation of Cromme's recommendation that management-board members' individual pay be disclosed is “catastrophic”, says Marco Becht at the European Corporate Governance Institute in Brussels.

In France, a series of official reports has suggested improved governance, proposing, for instance, that one-third of board members should be independent in companies where there is a controlling shareholder (for example, family businesses that go public). In October last year, MEDEF and AFEP, two business associations, jointly published a report on the governance of listed companies. It makes impressive reading. But it is not law.

On some fronts there has been progress. Last year, France introduced a law banning individuals from holding directorships in more than five separate companies. That led to a slew of resignations among directors who had appointed each other to their respective boards. But progress is being stoutly resisted by companies such as Michelin, which (like Parmalat) is quoted but also family-controlled. The tyremaker is almost the only big French company to have adopted none of the governance reforms recommended by the Viénot report on the subject in 1999.

What's more, France has a scandal of its own which may yet grow to Parmalat proportions. On December 23rd 2003, America's Securities and Exchange Commission (SEC) settled a court case brought against Vivendi Universal and two of its former French bosses, Jean-Marie Messier and Guillaume Hannezo. According to the SEC, the two men undertook a systematic fraud between 1999 and 2002, the year of Vivendi's eventual near-collapse, when they were ousted from power.

Arguably, this alleged fraud was less brazen than the scheme at Parmalat. But many of the mechanisms were the same. Vivendi's alleged wrongdoing relied on false accounting, inadequate disclosure and the use of complex deals between entities in a huge international group.

Let Brussels sprout?

To get reliable access to international financial markets and to regain investors' confidence, big companies in Italy and other European countries shaken by corporate scandal need to adopt better standards of governance. Given the international nature of the problem, it is not surprising that the European Commission is interested in the issue. In its Financial Services Action Plan (FSAP), published in 1999, the Brussels executive reviewed EU member countries' codes of corporate governance and argued that Europe's divergent guidelines on the subject remained an obstacle to the creation of a single capital market.

Patchy 2

Best-practice codes

	Britain	France	Germany	Italy	United States
Board independence	1/3 non-executive directors (NEDs), majority independent	Majority independent	Unspecified number of independents, max 2 ex-execs	Adequate number independent	Majority independent
Separate chairman/CEO	Split recommended	Do either	Required by law for larger companies	No	Not covered
Audit committee composition	At least 3 NEDs, at least 2 of them independent	2/3 independent	Minimal guidance	All NEDs	All independent NEDs
Executive pay disclosure	Yes	Yes	Encouraged	No	Yes

Sources: Davis Global Advisors; *The Economist*

At present, European Union (EU) countries have more than 35 governance codes of varying stringency. Britain alone has produced 11, and its governance rules are the most advanced, says Stephen Davis of Davis Global Advisors, a governance consultancy (see chart). The biggest difference in governance practices among EU members lies in the role of the employee and the strength of shareholders' influence.

In Austria, Denmark and Germany, the employees of companies of a certain size have the right to appoint some members of the supervisory board, while in France and Finland companies can allow workers to elect supervisory-board representatives. In all other EU countries a single-board structure is prevalent, with one or more managers running the company under the stewardship of a board of directors elected (for the most part) by shareholders.

The quality of transparency and disclosure across Europe is, at best, uneven, though things have improved since the introduction of tougher listing rules on national stock exchanges following the flotation of Europe's big bourses a couple of years ago. They will improve even more when a single set of international accounting standards (IAS) becomes compulsory for all EU companies next year.

Enforcing the new rules, though, is bound to be tricky. In some European countries there is still no enforcement of accounting standards at all. The most immediate concern of the International Accounting Standards Board (IASB), which created the IAS rules, is the approaching inclusion within the EU of eight former Soviet block countries, as well as Cyprus and Malta. Sir David Tweedie, head of the IASB, warned last week that the newcomers would struggle with IAS. Even some existing EU members in southern Europe could, he said, find it tricky to comply.

American regulators have long had a low opinion of European accounting and auditing. The Sarbanes-Oxley act was even extended to cover European companies listed in America because the SEC so distrusted European practices. Though the EU is about to introduce common standards, audit rules for European firms are still national, and the enforcement of accounting rules is generally pretty weak.

The drive for EU governance reform gained momentum in the wake of America's corporate scandals and the Sarbanes-Oxley act. In November 2002, a committee led by Jaap Winter, a Dutch law professor, presented its final report on corporate governance in the EU and the modernisation of company law to Frits Bolkestein, the EU commissioner for the internal market. In response to the Winter report, in May 2003 the European Commission published an action plan for improving governance in EU countries. In it, it identified priority areas for reform and fixed deadlines by when change should be achieved.

The plan does not call for Sarbanes-Oxley-style laws or the introduction of a pan-European governance code. That would have been unrealistic considering the EU's patchwork of national legal and regulatory systems. Moreover, in America the entire country was in shock after Enron and WorldCom and (more or less) willing to live with tough new laws. Each of Europe's recent scandals—Lernout & Hauspie in Belgium, Ahold in the Netherlands, Kirch in Germany, Skandia in Sweden, and now Parmalat in Italy—has thoroughly shaken only one of its 15 member countries. There has not been the cumulative effect that was felt in America.

A realistic road map

In the short term (this year and next) Brussels wants union members to focus on improving disclosure and shareholder communication, and on strengthening the role of independent non-executive directors. The commission is also suggesting that member states make the pay of company directors more transparent. Next month Mr Bolkestein will publish a proposal suggesting that each EU member state set up a national accountancy overseer, similar to America's Public Company Accounting Oversight Board, established by the Sarbanes-Oxley act to watch over the accountants who watch over the accounts.

In the medium term, from 2006-08, the commission is planning to get countries to reform multiple voting rights, golden shares, board structures and other more contentious issues. In the longer term, beyond 2009, Brussels policymakers are hoping to introduce another directive on company law. “It's a sensible road map with a focus on what is feasible,” says Holly Gregory of Weil, Gotshal & Manges, an international law firm.

Of course, expectations about corporate-governance reform need to be managed. Good corporate governance is not an insurance policy against fraud. Even very vigilant company directors, credit-rating agencies and investors can be duped by forged documents—but hopefully not for as long as seems to have occurred at the poorly governed Parmalat. The EU can only hope to make it more difficult for fraud to happen. But that in itself would be a welcome achievement.

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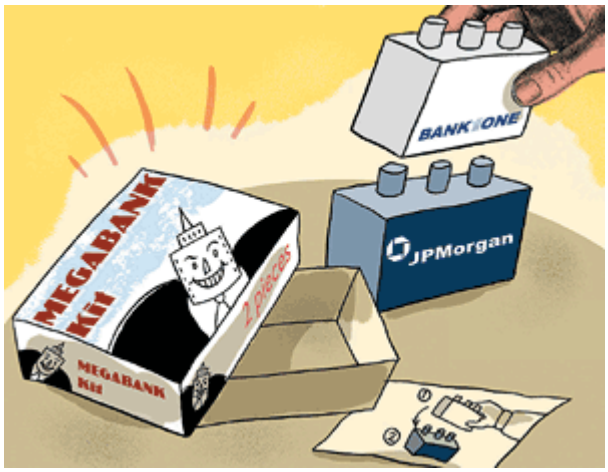
American banks

One fewer

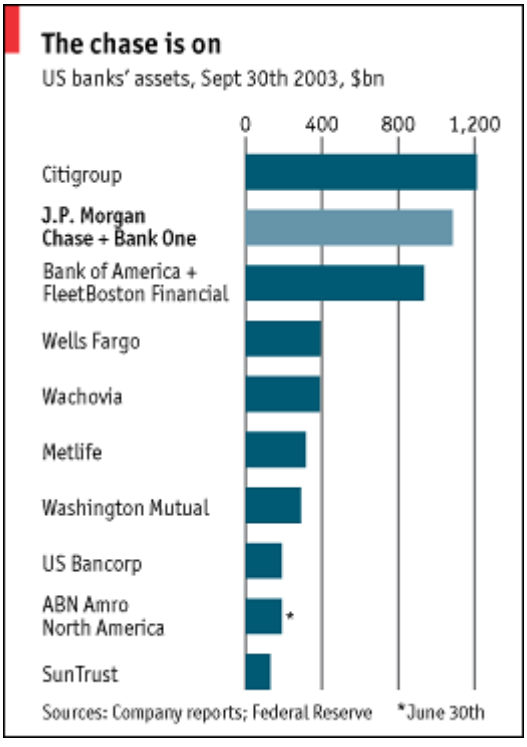
Jan 15th 2004 | CHICAGO AND NEW YORK
From The Economist print edition



Another huge American banking merger

AFTER a brief pause for the recession, America's banks are back to their favourite pastime: buying each other. On January 14th it was announced that Chicago's Bank One, a roll-up of the largest Midwestern banks, had accepted an offer from New York's J.P. Morgan Chase, itself the recent combination of four big institutions, for $58 billion in shares. This deal follows another big merger, that of Bank of America and FleetBoston, announced with much fanfare in October.

The latest combination will be a formidable one, with $1.1 trillion of assets, second in the American banking firmament only to Citigroup (and not that far behind—see chart). It will have 2,300 branches, combining Bank One's Midwestern network with J.P. Morgan's leading franchise in New York and smaller ones in Texas and Arizona. The new group will be a big asset-manager, overseeing $700 billion, and a leading credit-card issuer. The two banks have a one-third combined share of syndicated lending.



As well as combining the partners' strengths, however, the new firm will also have their weaknesses: a gap in investment banking and the threat of competition from innovative upstarts in retail banking—notably in Bank One's home town. Chicago is seeing a heated battle for retail customers' deposits. Washington Mutual, a Seattle bank, has moved into town aggressively in the past year. Last month the boss of Harris Bank, another competitor of Bank One's in Chicago, predicted that nearly half of all bank branches to open in America over the next few years will be in the city.

The deal is clearly a good one for the two principal bosses, J.P. Morgan's Bill Harrison and Bank One's Jamie Dimon. A year ago, Mr Harrison was taking a lot of stick from investors over the slow pace of integration between J.P Morgan and his own Chase Manhattan, following their merger in 2000. Business was poor, especially in investment banking, and the share price was feeble. Now Mr Harrison has pulled off another big deal, taking his institution to within spitting distance of Citigroup, the bank it most resembles in structure and scale.

The merger looks better still for the career of Mr Dimon, who is due to take over from Mr Harrison as chief executive of the new bank in 2006. Having helped Sandy Weill create the modern Citigroup and having been generally seen as Mr Weill's successor, Mr Dimon was purged by his mentor in 1998. He rejected many offers, including some from then-trendy new-economy firms, before taking over Bank One in 2000. Bank One was then reeling, having done one deal too many.

Mr Dimon quickly transformed a dysfunctional management, aided by the willingness of many of Citi's prized executives to flock to his side. Until this week's deal, however, it had seemed that Mr Dimon's resurrection may have run its course. In the days of his partnership with Mr Weill, an acquisition was the usual answer to stagnation. That looked an expensive option after Bank of America, the third-biggest bank in the United States, offered a huge premium for FleetBoston Financial late last year. This pushed up the likely cost of any purchase which Mr Dimon might have been considering.

Now, because Bank One is itself being bought, his shareholders will receive a takeover premium (of about 14%) instead of paying one. In his brief tenure, which spanned a sick economy and a stockmarket bust, Bank One's shares appreciated by two-thirds. Importantly for Chicagoans' self-esteem, the base for the merged bank's retail operation will stay in Illinois.

Nevertheless, there are some question marks over what the merger will achieve. First and foremost, the deal is about scale, especially in retail banking, so there will be few of the easy gains that come from eliminating overlapping operations. Strategically for Morgan, it has the disturbing characteristic of continuing the bank's tendency to follow trends: might it be that Bank of America's purchase of FleetBoston has focused Mr Harrison's mind?

Throughout the late 1990s when corporate finance was faddish, his Chase Manhattan built up its corporate bank at high cost through a series of acquisitions, notably of Hambrecht & Quist, a west-coast specialist in initial public offerings; the Beacon Group, a high level advisory firm; and then J.P. Morgan. The Beacon and Hambrecht deals were both outright disappointments and the marriage of J.P. Morgan and Chase never achieved what was hoped. Now, with retail banking once again in fashion, there has been a change of course. At the very least, a more distinctive strategy would have allowed for less costly deals. Perhaps more importantly, bank trends never seem to last very long, as many firms pursuing the same approach inevitably reduce returns.

Nuts and bolts

Despite this area of doubt, both banks' bosses are considered particularly good at retaining operational capabilities in chaotic times, notwithstanding the turmoil that inevitably follows big deals. Struggling to integrate J.P. Morgan and Chase Manhattan, Mr Harrison nevertheless cut costs quickly when revenues, especially in investment banking, did not meet expectations. During each of the mergers that created his bank, competing institutions formed groups to pick away clients lost in the shuffle, and had little success.

America's banking industry has now seen two big mergers announced within three months. More deals are likely to be in the works as banks seek both scale and broader geographical coverage, as they break out of their old regional constraints. The new J.P. Morgan Chase will still have branches in only 17 states. It is hard to believe that even the biggest banks would not like wider coverage. For the next tier, consisting of the biggest regional banks, the question of whether to buy or sell is becoming more acute all the while. And among America's smaller banks—the country has an impressive total of 8,000 banks—many mergers have been going on, without attracting the headlines generated by the biggest players' deals. Consolidation looks sure to continue. Who's next?

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Japanese bank reform

Reborn, remade, resold

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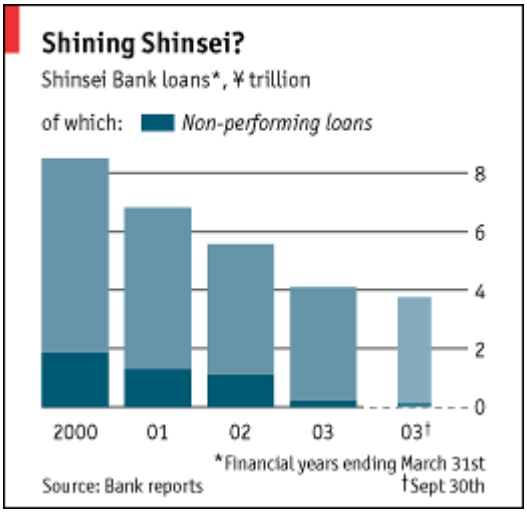
Shinsei, set to return to the stockmarket, does not provide a blueprint for reform

HAVING been the first foreigners to buy a Japanese bank, the owners of Shinsei Bank are preparing for another landmark: the first return of a once-nationalised institution to the stockmarket. This is a remarkable turnaround. Yet despite the dramatic clean-up of the bank's balance sheet, its long-term focus—and hence success—is far from assured.

Shinsei used to be the Long-Term Credit Bank (LTCB), which collapsed in 1998. The government spent almost ¥7 trillion ($66 billion) trying to restore its balance sheet. It was sold to Ripplewood Holdings, an American private-equity group, for ¥1 billion in March 2000. Reports suggest that if Ripplewood, which injected ¥120 billion into the bank, sold all its stake, it could make ¥1.5 trillion from the flotation, expected next month—a great deal for Ripplewood, not so great for the Japanese taxpayer. Ripplewood is expected to sell only about one-third of its stake.

Renamed Shinsei, or “new birth”, after its sale, the bank, led by its new president, Masamoto Yashiro, set out to shatter traditional Japanese banking norms. It built an information-technology system that other banks could only dream about. Instead of drab, utilitarian branches, Shinsei created stylish outlets—albeit only 29 so far—complete with colourful news screens and often with adjoining Starbucks cafés. It horrified local banks by sending wobbly borrowers into bankruptcy and by charging loan spreads that reflected risk.

Shinsei has managed to purge most of the old LTCB's bad loans. Its owners were given a “put” option, which expired last March. This allowed Shinsei to hand bad loans back to the government should they lose more than 20% of their value. Partly by exercising this option, Shinsei cut its ratio of bad to total loans from more than 20% to 4% by last September (see chart).



Still, Shinsei has yet to prove that it can create reliable, long-term sources of profit. So far its earnings have been bolstered by writing back the generous bad-loan reserves set up by the government, or by getting nervous fellow-creditor banks to buy its portion of bad loans rather than have Shinsei trigger a bankruptcy.

In the past three years the bank has slashed its total loans by half. When Japan's economy improves, and lending becomes profitable again, Shinsei may find it hard to rebuild its loan book. Other banks, which still do not price risk properly, are likely to undercut it. Customers might also be put off by Shinsei's reputation for being unsympathetic in difficult times. Shinsei has been better at attracting new depositors. Its small branch network, however, limits its ability to earn fees from selling products to retail investors.

Although Shinsei has been putting great effort into its investment-banking business, it faces tough competition from bigger rivals such as Goldman Sachs, Citigroup and Nomura Securities. LTCB's former network of regional banks, which might have brought in fresh clients, has all but disappeared, antagonised by Shinsei's aggressive policies.

More than five years after nationalising LTCB (and, two months later, Nippon Credit Bank), the Japanese authorities have still not decided what to do with the country's other banks. After those nationalisations,

the government soon went back to pumping public money into banks, but leaving in place the bosses who had caused the mess. It bailed out Resona, the fifth-largest bank, last May, then nationalised Ashikaga Bank, a regional institution, in November. Now it is drawing up a law that would make bail-outs easier, and avoid nationalisations or closures.

Perhaps the biggest lesson from Shinsei's experience is that reforming banks one at a time creates as many problems as it solves. After nationalising LTCB, the government could not bring itself to strip out all its bad loans before selling it. Other banks which had lent to the same bad borrowers would have been forced by the government's actions to downgrade their loans too. This would have implied a need for a dramatic increase in reserves, which the banks could not afford. So the government feared that cleaning up LTCB could lead to failures at other banks.

Shinsei's put option unexpectedly made things worse. Other banks, fearing that Shinsei's exercising the option would precipitate bankruptcies, bought its exposure, making their own troubles worse. Shinsei's sale did not end forbearance for many of its borrowers; it merely transferred the problem to other banks.

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Mutual funds

Seller beware

Jan 15th 2004
From The Economist print edition

The system of selling mutual funds finally becomes a target of regulators

FOR decades, mutual-fund companies and brokers have been up to things that were ethically suspect, but permitted nonetheless. Now regulators are not so tolerant. On January 13th the Securities and Exchange Commission (SEC) announced the results of an examination begun last April: eight broking firms and 13 fund companies improperly pushed mutual funds for which sales incentives were at best obliquely disclosed. No firms were named, presumably because formal litigation has yet to begin.

A day later, the SEC proposed new rules intended to stop the worst fund improprieties spotlighted in recent months. Independent directors will have to make up 75% of funds' boards; one must be the chairman. These directors must be able to hire their own staff. The SEC also proposed more disclosure of fund companies' payments to brokers and a code of ethics for investment advisers.

To industry observers, the most shocking revelation to emerge from the SEC's investigation was that even one broker refused inducements to push certain funds (another took the money, but did not promote the product). Again, no names have been revealed, so the saintly and the sharp remain secret, at least for now.

Sales of mutual funds have long been plagued by conflicts of interest. In theory, the fiduciary obligations of fund companies and fund sellers are clear. Fund companies are supposed to act in the interest of their existing shareholders. Sellers are supposed to act in the interest of their customers. In reality, broking firms have every reason to push in-house products, thus earning fees from sales and management, or outside funds carrying high commissions. The SEC's investigation revealed what was widely known: fund sponsors buy “shelf space” by directing trades in securities owned by their funds (and hence commissions) to brokers willing to give prominence to those funds. Other methods that were not mentioned by the SEC this week are being investigated. These include “soft dollar” arrangements, which eat into returns not through fees but through the prices at which securities are bought and sold.

Protection for customers rested on laws that required funds to disclose their aggregate fees clearly. Until now, however, brokers have not had to disclose what they are paid to sell a fund. Morgan Stanley, which pushes in-house products especially hard, recently settled charges that it improperly provided rich incentives for brokers to sell a particularly costly fund.

Under the SEC's plan, this will now change. Customers will be deluged with information on sales charges. Funds' boards will have to be reorganised. All of these changes address obvious shortcomings in an important industry. Inevitably, however, they will mean extra expense for the virtuous as well as the venal: think of the money that might be spent on independent directors' staff. This, in turn, will mean depressed returns for investors. That may be a scandal in itself.

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Deutsche Bank

Ackermann's trials

Jan 15th 2004 | FRANKFURT
From The Economist print edition

A heap of trouble for Germany's top bank, just when it was doing so well

THESE are hard times for Deutsche Bank, despite its huge strides in investment banking. Next week its chief executive, Josef Ackermann, goes on trial in Dusseldorf. Careless words by Rolf Breuer, the head of its supervisory board, led to another court ruling last month that may cost Germany's biggest bank several hundred million euros in damages. Then there is Parmalat. Although no evidence has emerged of complicity in the Italian dairy group's fraud, Deutsche's name has become entwined in the affair.

In many other respects, however, Deutsche's reputation has never been higher. In dubbing it “Bank of the Year 2003”, *International Financing Review*, the capital markets' favourite newssheet, purred that Deutsche was a “lean, aggressive, focused universal bank”. In the league tables that investment banks watch so keenly, Deutsche excelled last year as lead manager of bonds and convertible bonds and of some racier products, such as repackaged debt securities and high-yield “junk” bonds. In other disciplines it rarely fell below the top ten in the world.

AP

Ackermann's still smiling

However, it is still nowhere near the top in equity offerings and advice on mergers and acquisitions, except in Germany. It still has a problem with costs, which were a fat 82% of income in the third quarter of 2003, thanks mainly to the thick pay packets of its investment bankers and its poor returns from corporate and retail banking.

Mr Ackermann must try to improve the weak spots while spending two days a week, probably until June, in a courtroom. He and four others face charges of “breach of trust” over the way bonuses were awarded to board members of Mannesmann, a telecoms company, after its takeover by Vodafone in February 2000; another is charged as an accessory. Mr Ackermann sat on Mannesmann's supervisory board. There is no suggestion that he gained personally. But he and Deutsche must face a long-drawn-out trial, with the risk of uncomfortable revelations about sloppy procedure.

Nor was there any harmful intent in Mr Breuer's remarks in a television interview about the financial health of the Kirch media group shortly before its bankruptcy. But he was careless, and a Munich court found Deutsche (but not Mr Breuer) liable for damages, to be set in due course, without right of appeal. The bank said this week it has lodged a protest with the federal supreme court in Karlsruhe. Meanwhile, Kirch has filed a suit against Deutsche in America.

Deutsche's involvement with Parmalat also looks sloppy. It led a €350m ($393m) bond issue for the group in September. It was also a leading borrower and lender of Parmalat shares, so that in November it technically held the voting rights to over 5% of Parmalat stock. That stake had fallen to 1.5% by December 19th, the day the dairy company's black hole became public. It reported this, perhaps over-zealously, to the Italian authorities. That may have given the wrong impression, say sources close to the bank, because the transactions were for third parties.

Deutsche had other relationships with Parmalat. Massimo Armanini, Deutsche's top investment banker in Italy, worked for the company from 1998 to 2000. Deutsche's investment bankers have a mandate to auction Parmalat's North American bakery subsidiary. The bank's ratings-advisory team helped Parmalat draft a presentation to Standard & Poor's, a rating agency, in late November, to answer concerns about suspected liquidity problems. The presentation document sported the logos of both Parmalat and Deutsche—without Deutsche's permission, the bank insists.

Carelessness, rather than complicity, perhaps. Nevertheless, an American law firm, Milberg Weiss Bershad Hynes & Lerach, is launching a class-action lawsuit in New York on behalf of Parmalat investors. Deutsche has not been named in the suit, but Darren Robbins, a spokesman for the law firm, says that the bank is “in it up to the eyeballs”.

This is awkward for a bank that managed to avoid most serious attacks on conflicts of interest that beset the investment-banking industry following the collapse of Enron in 2001 and the bursting of the tech-stock bubble. Mr Ackermann will need a clear head to steer the bank through the coming storms.

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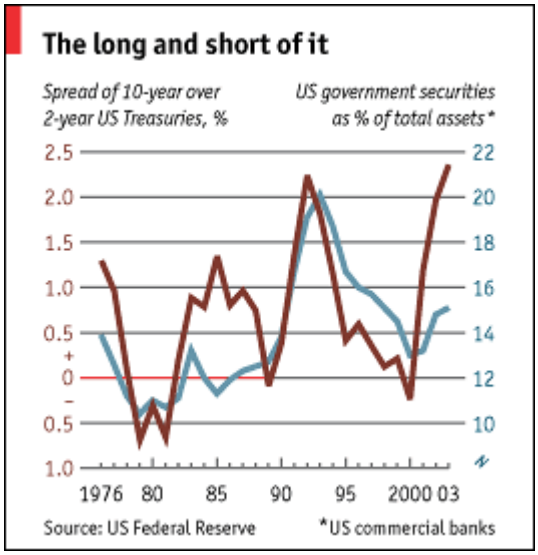
Treasury bonds

Wrong-footed

Jan 15th 2004
From The Economist print edition

Why have Treasury-bond yields fallen?

ALTHOUGH they are almost as hated as the dollar by fund managers, American Treasury bonds have not performed as dismally of late. Quite the contrary: in the past week the price of bonds has jumped, taking the yield on the benchmark ten-year bond to a sniff under 4%—and lower than it was at the beginning of last year. This is odd. The ten-year bond yield is, in essence, America's and the world's long-term risk-free interest rate. A year ago, economists and investors were fretting about anaemic growth and deflation in America. Since then, growth and the appetite for risk have soared. So, at first, did yields on ten-year bonds. Now they are falling again sharply. Why?



The latest fall in yields was sparked by a report on January 9th which showed that far fewer jobs are being created—only 1,000 in December—than economists had expected, and raised renewed fears about an unsustainable “jobless” recovery. A parade of Fed officials said again that interest rates might have to stay low for a “considerable period”.

Although pessimism on jobs may be overdone (see article), markets seem to believe the talk of interest rates remaining low. At the peak last September, the futures market was predicting that short-term interest rates would rise to over 3% next December. Now it thinks that they will be less than 2% because heady growth has not sparked inflation; indeed, it continues to fall. Consumer prices rose by only 1.9% in the year to December. The falling dollar should push up the price of imports, but there is no sign of that yet.

Plenty of investors need to buy Treasuries for reasons only loosely connected with growth worries. Asian central banks have been buying billions of dollars to stem the rise of their own currencies and have invested the money mostly in Treasury bonds and bills. The Bank of Japan has been the most aggressive. Last year, it intervened more heavily than any central bank in history, buying $187 billion and bringing its total foreign-exchange reserves (mostly held in dollars) to $674 billion. So great has been the desire of Asian central banks to keep a lid on their currencies that they now have reserves of $1.8 trillion, much of it parked in Treasuries.

Quite how much more they will want is a moot point. A recent rule change means that the Bank of Japan is allowed to buy another $600 billion or thereabouts of foreign currency. But even if Asian demand wanes, the appetite of another group of investors appears to be waxing: America's banks.

There are many good reasons why banks are adding to their stock of Treasuries. The first is that the yield curve—the difference between short and long-term rates—is historically very steep, which makes it much more profitable to borrow short and buy long-dated securities.

There is, moreover, a dearth of such assets. Lending to companies is shrinking. At the beginning of last year, there were $954 billion of corporate loans outstanding; now there are $884 billion. Eager to repair tattered balance sheets, companies have been investing from profits rather than borrowing the money from banks. The supply of mortgage-backed bonds is also drying up because fewer people are refinancing mortgages. Banks' holdings of mortgage bonds have fallen from almost $400 billion to just over $350 billion.

And then, of course, there are the fund managers with fewer long-dated Treasuries in their portfolios than their benchmarks require. This would have been splendid if bond prices had fallen. But they have gone up. Given how many investors want to buy them, the wait for a sharp fall could be a long one.

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Morgan Stanley and LVMH

Handbagged

Jan 15th 2004 | LONDON AND PARIS
From The Economist print edition

A French court's verdict is a blow to independent investment research

BERNARD ARNAULT, the chairman of LVMH, a luxury-goods conglomerate, has scored a personal victory in his long-running feud with Gucci, another stable of posh brands. On January 12th a Paris court ordered Morgan Stanley to pay LVMH €30m ($38m) in compensation for alleged bias in its investment research on the company. The motive, says Mr Arnault's camp, for luxury-goods analyst Claire Kent's "systematic denigration" of LVMH was its lucrative advisory work for Gucci. With Morgan Stanley's help, Gucci foiled a takeover attempt by LVMH a couple of years ago.

LVMH is casting itself as a de luxe version of Eliot Spitzer, New York state's indefatigable prosecutor. It regards its success as a blow against investment banks' conflicts of interest between their advisory work for firms and research for investors. In fact, the result may be to make research even less useful, if companies threaten to sue whenever they disagree with an analyst. On January 13th Sodexho Alliance, a catering firm, said that it might sue Citigroup over the bank's coverage of its stock.

Ms Kent certainly said unkind things about LVMH. She argued that the Louis Vuitton handbag brand may have reached "maturity". She also raised the possibility of a downgrade of the group by Standard & Poor's, a credit-rating agency that had placed LVMH on "negative outlook." And she reminded investors that LVMH had "destroyed value" when it lost money investing in Sephora, a cosmetics chain. But it is hard to see how this amounts to *fautes lourdes*, or gross tort, as the court found.

Lawyers familiar with the matter say the evidence would not have been enough to make a case against Morgan Stanley in America or Britain. For instance, there was no damning e-mail by analysts of the kind that got Merrill Lynch and a star analyst, Henry Blodget, into hot water for hyping internet shares to the public while saying something different internally.

Might politics have helped secure a decision for the home side? France is still reeling from the fallout in America of its stand against the war in Iraq. France is also forking out at least $585m to avert a criminal trial for the fraudulent purchase by Crédit Lyonnais, a French bank, of Executive Life, a Californian insurer, in the early 1990s. This has left French nerves raw, perhaps even those of French judges.

Morgan Stanley said it will "appeal, appeal, appeal". Meanwhile, the court has appointed experts to assess whether LVMH deserves even greater damages. Mr Arnault could well be laughing all the way to the bank.

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The Starbucks index

Burgers or beans?

Jan 15th 2004
From The Economist print edition

A new theory is percolating through the foreign-exchange markets

Get article background

STARBUCKS was due to open its first coffee shop in France on January 16th—a brave step, given that Paris invented café culture. Some of the French press are frothing at the mouth at the notion that Americans think they can make coffee. Jean-Paul Sartre, they scoff, would hardly have found the same inspiration slurping from a paper cup as sipping black coffee in Les Deux Magots. *The Economist*, however, has been pondering a more existential idea: what can the price of Starbucks coffee—now served in as many as 32 countries—tell us about exchange rates?

Readers may be familiar with *The Economist*'s long-running Big Mac index: by comparing burger prices around the world, it offers a light-hearted guide to whether currencies are at their "correct" level against the dollar. Given the dollar's recent plunge against the euro and growing complaints that China is unfairly holding down its currency, we cannot resist testing whether a Starbucks "tall latte index" reaches the same conclusions as our Big Mac index. Both are based on the theory of purchasing-power parity (PPP). This says that, in the long run, exchange rates should move towards levels that equalise the prices of a basket of goods and services in different countries—ie, a dollar should buy the same everywhere.

Our hot tips

Local currency under (-)/over (+) valuation against the dollar, %, using:

	Starbucks tall-latte index	McDonald's Big Mac index
Australia	-4	-17
Britain	+17	+23
Canada	-16	-16
China	-1	-56
Euro area	+33	+24
Hong Kong	+15	-45
Japan	+13	-12
Malaysia	-25	-53
Mexico	-15	-21
New Zealand	-12	-4
Singapore	+2	-31
South Korea	+6	0
Switzerland	+62	+82
Taiwan	-5	-21
Thailand	-31	-46
Turkey	+6	+5

Source: *The Economist*

By coincidence, the average price of a Starbucks tall latte in America is the same as the average price of a Big Mac, $2.80. By dividing the local currency price in each country by the dollar price we can calculate dollar PPPs. Comparing these with actual exchange rates is one test of whether a currency is undervalued or overvalued.

Our tall-latte index tells broadly the same story as the Big Mac index for most main currencies (see table; see article). Economic trouble is surely brewing in Europe: the euro (based on the average price of €2.93—$3.70—in member countries where Starbucks operates) is about 30% overvalued against the dollar. Sterling is 17% too strong. By both measures, the Swiss franc is the world's most overvalued currency. The Canadian, Australian and New Zealand dollars are still undervalued against the dollar despite their recent climb.

Where the two measures differ is in Asia. The burger index says the yen is 12% undervalued against the dollar; on the coffee standard, however, it is 13% overvalued. More startling is the Chinese yuan: it is 56% undervalued according to the Big Mac, but spot on its dollar PPP according to our Starbucks index. If so, American manufacturers have no grounds to complain about the yuan. The pricing differences probably reflect different competition in the markets for the two products.

Many readers will find burgernomics and lattenomics hard to swallow. Both are flawed as measures of PPP, because they are distorted by differences in the cost of non-tradables such as rents. Yet they are surely a more fun way to understand exchange rates than textbooks. Many readers ask why we don't we use the price of *The Economist* around the globe. Unlike the Big Mac or a tall latte, *The Economist* is not

produced locally in lots of countries, so distribution accounts for a large chunk of its cost. Burgers and coffee are therefore likelier to give some clues about currencies.

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Zimbabwe's banks

Crisis breaks

Jan 15th 2004 | JOHANNESBURG
From The Economist print edition

What a surprise

Get article background

ROBERT MUGABE, Zimbabwe's president, wants to cut inflation from 700% or so, as he has heard that it makes life hard for the little people. Last month, his new central bank governor, Gideon Gono, lifted interest rates to roughly the level of inflation, choked the money supply and told the worst banks and asset-management firms to expect tighter regulation, and no bail-outs if they go bust.

That pushed some institutions to the verge of collapse. Last week seven of the country's 17 banks could not clear their books. Depositors fled, and shops refused their cheques. If Mr Gono had stuck to his guns, there would have been a shake-up. But under pressure from politicians, who are quite chummy with a certain type of banker, he has said that he might rescue wobbly banks after all.

Those who need a lifeline mostly do not deserve one. Some institutions won licences through political connections, and returned the favour by lending money to ruling-party cronies. Others appear to have been operating without any kind of licence, and to have spent their depositors' money on flash cars, posh houses and, literally, on big piles of bricks.

With inflation rocketing and businesses everywhere going bust, such investments may have made sense. But amid the confusion, some managers have been up to no good. This week, one of the ruling party's leading tycoons, Philip Chiyangwa, was arrested in connection with a scandal at an asset-management firm called ENG. Some 18 luxury cars, possibly owned by ENG, were found at his homes. He denied any wrongdoing.

Mr Gono has little room for manoeuvre. Dropping interest rates will buy time for some banks, but it will also push up inflation. As investigators dig, they are likely to find more fraud, so several banks will either merge or collapse, says John Robertson, an economist in Harare, Zimbabwe's capital. Banks with foreign parents will survive, as customers believe they are safe. But the rest?

Meanwhile, the real economy continues to implode. The rate of increase of inflation may slow, but it is still likely to top 1,000% by mid-year, believes Mr Robertson. As the country has de-industrialised, output depends increasingly on the rain. Mr Mugabe may not be able to command the clouds, but he did promise this week to stamp out corruption. Phew.

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Economics focus

Rational extremists

Jan 15th 2004
From The Economist print edition

Are violent religious groups guided by an invisible hand?

PEOPLE who take their religious faith to violent extremes have achieved new notoriety in recent years. As it happens, many of the terrorist atrocities in the Middle East, America and Asia have been sponsored by Islamic radicals. The Taliban, for example, took control of Afghanistan in the 1990s, imposed a strict, religious system of government and created a haven for al-Qaeda. In Israel and the Palestinian territories, Hamas has been one of the most effective terrorist groups, by the grisly measure of success in suicide attacks.

On the face of it, such groups' activities stem from simple obedience to a warped perception of God's will. However, social scientists have more sophisticated and perhaps more convincing explanations, drawn from politics, sociology or anthropology. What on earth, you might ask, can economics add? Plenty, according to a new paper* by Eli Berman of the University of California at San Diego. Mr Berman, indeed, puts economic motives at the centre of extremist activity.

God and Mammon

To be sure, strict religious observance of any faith—violent or not—sits awkwardly with economics. Cults and sects typically require their members to eschew worldly pleasures and goods, to an even greater degree than mainstream faiths. Devotees are asked to make costly sacrifices and obey orders to the letter. Most economic theory, on the contrary, starts from the idea that you can never have too many material comforts.

Although ascetic behaviour is intended to reap rewards in the afterlife, Laurence Iannaccone, now of George Mason University, observed a decade ago that it can pay off handsomely in this world. By studying American Christian groups such as the Amish, who forgo modern technology, and the Mormons, who give years of their life as missionaries, he calculated that the costs of religious membership are, despite the sacrifices, lower than the benefits received.

What are these benefits? Religious groups often provide their members with what economists call “club goods” or “public goods”, such as mutual insurance, education and—when the state is ineffective—even law and order. Prohibitions on working outside the sect and on wasteful pleasures serve as a kind of tax that keeps human and financial resources devoted to the group, in much the same way that government taxes finance public services. Moreover, Mr Iannaccone found that the stricter a religious sect is, the more public goods it provides. All this fits in well with economic theory.

Mr Berman's paper applies this lesson to the Taliban and Hamas, arguing that a similar economic logic might be at work. After all, he notes, these groups also provide many public goods. The Taliban restored law and order, of a sort, to Afghanistan. Hamas's affiliates provide health care and schooling. Extremist groups also seem to weigh carefully the costs and benefits of their ideologies and terror strategies.

He also argues that extremist groups are likely to be especially efficient at running a militia, because militias are prone to the risk of defection. Religious extremists can extract signals of high commitment from their members. They may require them to demonstrate their devotion to the cause by studying holy texts for years or by committing acts of destruction, of which suicide attacks are the most extreme example.

Mr Berman's analysis does not apply exclusively to Islamic groups. Militias, he says, have sprung forth

from religious movements going back at least to the Crusades. Mr Berman points to another sect, the Gush Emunim, a movement of orthodox Jews that gave rise to the Jewish Underground, an Israeli militia that was active in the late 1970s and early 1980s. Like most extremist groups, it tightly regulated its members' lives, from their dress to their housing arrangements. Yet this group failed to maintain its strength. Perhaps this was because, being comprised of citizens of Israel, a well-functioning state, it was not the sole supplier of public goods to its members.

If religious extremists obey economic laws, the future looks considerably brighter. Mr Berman reckons the policy implications are simple. In the West Bank and Gaza strip, for example, a functioning government that offers public goods such as schools, medical care and old people's homes should undermine Hamas. The power of the Taliban is similarly likely to be sharply reduced if and when public services are available to most Afghanis. His model fits with the commonsense notion that failed states and poverty are breeding grounds for terrorism.

Mr Berman points to many of the weak or failed states in the world where public services are paltry or non-existent, such as Somalia, Algeria, Chechnya and the Philippines, as likely places where extremists are trying to fill the gap. One notable exception to his theory is Saudi Arabia. Despite a rich government that provides generous services, extremist militia activity persists. Another exception seems to be some of al-Qaeda's terrorists, who have been neither poor nor deprived of public goods.

As economics has moved into ever farther-flung realms, it seems that nearly every human activity—now even religious extremism—is falling under its scrutiny. This might sometimes stretch economics too far. Yet Mr Berman is in good company. He points out that Adam Smith, commenting on religious sectarian strife in 18th-century Europe, recommended similar government intervention. Smith favoured “frequency and gaiety of public diversions” financed by the state to distract the people from “disagreeably strict” religious sects. Sadly, in too many places gaiety is in short supply.

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* “Hamas, Taliban and the Jewish Underground: An Economist's View of Radical Religious Militias.” NBER Working Paper 10004 http://www.nber.org/papers/w10004

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About sponsorship

America's space programme

Pie in the sky

Jan 15th 2004
From The Economist print edition

Science Photo Library

America's space agency is to return to the moon. Not everyone is happy about this

Get article background

LOSING the shuttle *Columbia*, and its crew of seven astronauts, was a serious blow to America's National Aeronautics and Space Administration (NASA). As with all mishaps of this scale, it caused a great deal of navel-gazing. One result was an excoriating report, last year, on the way the agency works. The second was President George Bush's announcement on January 14th that America will return to the moon, and prepare for trips further afield in the solar system.

Mr Bush announced merely the broad brush-strokes of his “vision”. The details will be painted in later. But anyone who is thrilled by the idea of an extended return to the moon would do well to remember that in 1989, on the 20th anniversary of the first moon landing, Mr Bush's father, then president, announced something rather similar. Cost estimates for that plan turned out to be so astronomical ($400 billion) that Congress quickly buried the idea.

The current President Bush's plans are more modest. They begin with the landing of unmanned spacecraft on the moon by 2008, in order to lay the groundwork. An “extended human presence” on the moon (there was no actual mention of a permanently manned moon base) would be established sometime between 2015 and 2020. This would make use of a new “Crew Exploration Vehicle” that would be developed and tested by 2008 to be ready to take over servicing the international space station in 2010 when, as Mr Bush also announced, the space-shuttle fleet would be withdrawn from service. Mr Bush did not say that the Crew Exploration Vehicle would be re-usable, and cynics might suspect that he is actually proposing little more than a souped-up version of the Apollo craft that formed the core of America's previous moon venture.

That would not necessarily be a stupid idea. One expensive lesson of the shuttle programme is that trips into space are too infrequent to justify building a re-usable spacecraft. Roger Pielke, a science policy researcher at the University of Colorado, estimates that the space shuttle cost America $150 billion (at 2002 prices) between its birth in 1971 and the present day.

And cost, of course, is an issue. The plans Mr Bush outlined would be paid for by reallocating $11 billion of NASA's existing budget over the next five years, and adding $1 billion of new money. Mr Bush did not

say which programmes would suffer cuts, but given that the shuttle and the space station are to plod along intact, there is a clear risk that the agency's successful scientific programme will bear the brunt.

It remains, of course, for Congress to approve the plans. But, given that Mr Bush is asking for only a little extra money and that he is proposing eventually to scrap the unpopular shuttle, he might just swing it. Whether this would really advance America towards the goal of travelling further afield, to Mars and beyond, is a moot point. There was the usual guff in Mr Bush's announcement about using materials mined on the moon to make rocket fuel and air for longer-range expeditions. But, wisely, Mr Bush did not commit himself, and left decisions on such matters to future presidents, and the future Congresses that will have to approve their cost.

Privatise it

One might expect space enthusiasts to be thrilled about a return to the moon. Perhaps they would be in different circumstances, but not under the current management. The Space Frontier Foundation is an organisation “dedicated to opening the space frontier to human settlement as rapidly as possible”. But as news of the plan leaked out, it warned that NASA was “bloated, inflexible, self-indulgent and lives on the re-runs of its better days”. The agency can only succeed, said the foundation, with the involvement of the private sector, handing over the baton at the right moment.

That could yet happen. For even now, dozens of teams of entrepreneurs are racing with each other to build a working spacecraft with relatively small sums of money and no help from the government. They are competing for what is known as the X-Prize, a $10m reward for the first craft capable of taking tourists into space. That may sound like pie in the sky, but last month one of the contenders took a test craft to supersonic speeds. It was the first manned supersonic flight by a craft developed by a truly private effort.

Even on today's calculations, a little bit of space tourism looks to be worthwhile. Hundreds of people have already put down cash deposits for a trip to the edge of space with a company called Space Adventures, of Arlington, Virginia. This firm (which already arranges $20m journeys to the space station, on board Russia's *Soyuz* craft) is offering trips with whichever X-Prize contender first starts commercial operations. These trips ($100,000 each, in case you want to join in) will take passengers to the edge of space, rather than all the way into orbit. But space tourists will still experience weightlessness, see the Earth from a rather special vantage point, and qualify as astronauts.

This is not exactly a grandiose vision compared with a manned base on the moon. But it is a more realistic one and, if successful, it can be built upon. NASA has done great things, of the sort that private enterprise would not and should not cough up for, with its unmanned scientific space missions. It should concentrate on those and leave the business of putting people into space to business itself.

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The evolution of disgust

Tunbridge Wells strikes back

Jan 15th 2004
From The Economist print edition

Disgust, as many suspected, is a disease-avoidance mechanism

TELEVISION is often viewed (at least by intellectuals) as an anti-intellectual medium. But truly clever people know how to harness even the most unpromising material, and that is what Val Curtis and her colleagues at the London School of Hygiene and Tropical Medicine have done. They employed the mass-market appeal of TV to test a long-held, but unproven, hypothesis: that the emotion of disgust evolved to protect people from disease.

They set up their experiment in October 2002, by publicising it on a BBC programme called “Human Instincts”, which was presented by Lord Winston, a well-known British doctor. Viewers were invited to visit a website and, after giving a few biographical details, to view a series of 20 pictures and rate each of them for disgustingness on a scale of one to five. They were also asked to choose, from a list of possible candidates, with whom they would least like to share a toothbrush.

Six of the pictures were not part of the experiment. The others were members of pairs, with one element of a pair depicting a “disease-salient stimulus”, while the second—of which the first was often a photomanipulation—was intended to be as similar as possible, but without the disease salience. All 20 pictures were mixed up and presented at random to the experimental subjects, of whom (after obvious frauds such as people claiming to be under five years old were removed) there were almost 40,000.

The results have just been published in the *Proceedings of the Royal Society*. In all seven pairs, the disease-salient pictures were more disgusting than their counterparts. For things like the apparent depiction of bodily fluids, or of a face that had been “enhanced” with spots, that may come as no surprise. But a crowded railway carriage was more disgusting than an empty one, and a louse more disgusting than a wasp.

These last results confirmed Dr Curtis's suspicion that disgust is not, as many disgustologists believe, just a way of avoiding eating disease-bearing materials. Rather, it extends to threats that might be contagious—in other words might be, or carry, what children refer to as “cooties”, as has been suggested by Steven Pinker, a psychologist at Harvard University.

Indeed, one result of the study was to show that the young are easier to disgust than the old (so the idea that the most easily disgusted individuals are typified by elderly colonels living in the leafy suburban town of Tunbridge Wells is wrong). Another result was that women are more easily disgusted than men. Both of these make evolutionary sense. The young have more reproductive potential than the old, so should be more careful about what they touch and eat. And women are usually lumbered with bringing up the children, so have to be disgusted on their offspring's behalf, as well as their own.

The results of the toothbrush study made similar sense. Strangers are more likely to carry novel germs than acquaintances. Hence, of the available choices of toothbrush partner, a postman came off worst, and a lover best. A brush notionally belonging to a weatherman was, however, preferred to the boss's. Clearly the British feel more affinity with the former than the latter. Perhaps it might have been instructive to include a famous television personality among the choices?

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AIDS statistics in Africa

Good news, apparently

Jan 15th 2004 | JOHANNESBURG
From The Economist print edition

Building better models of the prevalence of HIV

APART from Uganda, where HIV infection rates have been falling for several years, there has been little to celebrate about AIDS in Africa. For much of the past decade scientists repeatedly lifted their estimates of the numbers of Africans who were infected with HIV and of how many would die from it. Early hopes that prevalence rates would peak at a quarter of any adult population were dashed by data from Swaziland and Botswana that showed more than one in three adults now carry the virus.

But preliminary results from the quinquennial Kenya Demographic and Health Survey (KDH) have brought unexpected good news. This survey, carried out last year by the Kenyan government with the assistance of America's Centres for Disease Control and Prevention (CDC), suggests HIV prevalence is significantly lower in Kenya than was previously believed.

Two years ago UNAIDS, the United Nations agency charged with combating the disease, said it thought 2.3m adult Kenyans were infected with HIV (plus 200,000 children). That suggested an adult prevalence rate of 15%, though the agency has now revised its estimate down to 9.4%. But the new data cut the figure still further. They suggest a rate of 6.7%. That means just over 1m adults are infected. If the survey, and the model of measuring HIV that it uses, pass further scrutiny when they are published in full later this year, it would also hint at lower prevalence rates elsewhere in Africa.

There are—as UNAIDS points out—reasons for caution about the new result. This was the first time that the KDH survey included an HIV test, so comparison with previous years is not possible. Members of 3,000 households were asked to give blood for tests for HIV, but just 70% responded. More needs to be known about those who refused to take part or who were absent—perhaps even dead of AIDS. And some results are surprising, most notably the figure of 4.5% HIV-prevalence among men, half that found in women.

There are reasons to expect a lower rate in men than in women. Male circumcision helps prevent infection, and women are vulnerable to rape and also tend to have sexual partners who are older, and therefore more likely to have picked the virus up at some point during their lives. However, even in combination these things would not be expected to result in such a stark discrepancy between the sexes. That discrepancy may therefore show a weakness in the study's design.

Nevertheless, a survey that draws its data from a sample of the whole population is likely to be more accurate than previous ones that relied on testing pregnant women for HIV and then extrapolating. And an article published last month in the *Lancet*, by Ties Boerma of the World Health Organisation and his colleagues, argues that the bias is systematic. According to Dr Boerma, models based on antenatal surveys (so called “sentinel” models) estimate HIV prevalence to be “about a quarter higher” than do models based on blood tests of the general population (known as “population-based” models).

Dr Boerma reviewed the results of population-based general-health surveys similar to Kenya's that were carried out in Zambia and Mali, and also a study based on saliva samples that was carried out in South Africa. The Zambian study suggested a 15% rate in 2002, compared with a UNAIDS sentinel estimate of 21.5% that had been made the previous year. In Mali the new and old figures were about the same, at 2%. In South Africa a rate of 16% was found in 2002, down from a UNAIDS sentinel estimate of 20% the year before. And a second, smaller, population-based study carried out in Kenya last year suggested 1.4m-1.8m adults are infected—more than the KDH value, but less than the original sentinel model would have it.

Refined models using sentinel studies are starting to suggest that estimates of prevalence in the late

1990s were probably too high in several other countries as well, according to Kevin DeCock, the head of the CDC's Kenyan operation. That opens the question of how much the current UNAIDS estimate of 26.6m HIV infections in sub-Saharan Africa might need to be reduced. If Dr Boerma's estimate is correct, a figure of 21m may be closer to the truth.

That would not be the only revision in an optimistic direction that has taken place recently in the field of AIDS. Rian Malan, a South African writer, recently documented how models used to estimate the number of deaths from the disease have been abandoned in quick succession as they have failed to track changes in mortality rates. An early one, Epimodel, estimated 250,000 AIDS deaths in South Africa for 1999 alone. More recent models, using slightly lower figures for HIV prevalence rates, deflated estimates for that year first to 145,000 deaths and then to 65,000. (The true number remains mysterious, since cause-of-death data collected in the country are insufficiently reliable. However, the total number of deaths in South Africa in 1999 was 375,000.)

Mr Malan suggests, from this continual downgrading of the death rate, that AIDS activists, donors and others may have exaggerated the problem to raise money and get governments to act faster. A conspiracy seems unlikely, however, since the new figures still describe an awful epidemic—even 21m cases would be 21m too many. Instead, these figures reflect improving skills at modelling a new disease accurately. If that means fewer people are doomed than once thought, it is good news indeed.

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A robot scientist

As ye sow...

Jan 15th 2004
From The Economist print edition

A machine can now do science

FROM the Luddites onwards, workers whose jobs have been destroyed by scientific advances have voiced their complaints loudly. Such people might be amused by a paper in this week's *Nature*, in which a group of scientists describe a way of automating science itself.

The robot scientist developed by Ross King of the University of Wales at Aberystwyth, and his colleagues, does everything a flesh-and-blood scientist does—or, rather, it does what philosophers of science say that scientists ought to do. That is, it formulates hypotheses from observations, conducts experiments to test them, and then formulates new hypotheses from the results. And worse, from the point of view of the human researcher, it does so as effectively as a person.

One of the biggest problems in modern science is making sense of the genetic data that are pouring into the world's databases from automatic DNA-sequencing machines. So Dr King and his colleagues chose to apply their robot to the problem of working out which genes do what. They decided to look at yeast genes, because yeast biochemistry is reasonably well understood (this was a test, not a search for new results). Their idea was to study a biochemical pathway whose intermediate chemical steps were known and see if their robot could identify the genes for the enzymes that control each step.

The way a human scientist would do this is to use a series of strains of yeast that have each had a known gene “knocked out” of them (these are available commercially). He would then try growing each strain in a nutritional medium that was missing one of the intermediate chemicals in the pathway. If the knocked-out gene was required to make that intermediate, the culture would not thrive, and a piece of the jigsaw would have been discovered.

Mostly, this is grunt work. The intellectual input comes from deciding, on the basis of the results obtained, which experiments to do next until you have filled in all the blanks. The robot scientist was able to do this. It was fitted with artificial intelligence software that could perform the logical processes involved in making such decisions, and this software was given a representation of the pathway chosen (one of those by which amino acids, the building blocks of proteins, are made) from which to work.

The software then sent instructions to the machine in which the yeast cells were being grown, to pick particular strains and mix them with particular media. Once the cells had been given enough time to grow, the machine automatically examined the cultures to see how opaque they were (and thus how well they had thrived). It then returned the results to the artificial-intelligence package, and awaited instructions about what to do next. Eventually, the package worked out what was what, and told its masters the result. And it did so in the same number of experimental steps as the best efforts of human researchers against whom it was pitted.

Though they chose genetics to test their idea, Dr King and his colleagues think it could be applied to other fields where vast numbers of small, fiddly experiments need to be done in order to arrive at a result—for example, drug design and certain sorts of advanced chemical synthesis. One question is, if their robot does make an important discovery, will it be eligible to win a Nobel prize?

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About sponsorship

Political thought

Ideas to live (and die) for

Jan 15th 2004
From The Economist print edition

A new history looks at the movements that shaped the world

ONE remark of John Maynard Keynes on which political thinkers, whatever their stripe, will surely agree is this:

> The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed, the world is ruled by little else. I am sure that the power of vested interests is vastly exaggerated compared to the gradual encroachment of ideas.

You can record the 20th century as a story of astonishing technical progress. You can tell it as the rise and fall of powers, or as the painful recovery from modern society's relapses into barbarism. But if you leave out ideas, you leave out what people were ready to live and die for.

All the stranger, then, that for years there were so few good histories, in English, of political ideas. One lonely work was “Western Political Thought” by John Bowle, a master at Westminster School in London. The book began in Mesopotamia and ended with Rousseau. Published in 1947, it was essentially the work of a learned and very widely read amateur. Indeed, professionals in the subject scarcely existed. Though dated, the book is still valuable, with flashes of Bowle's anti-authoritarian character, which so appealed to his clever young charges. After a particularly heavy night he would send a poet friend, John Betjeman, to take his classes. “Mr Bowle”, Betjeman would explain, “is having a difficult morning.”

Gone are those days. Professional historians have long since carved out a specialism of their own, nowhere more than at Cambridge. The university has become a centre for the history of political ideas led by Quentin Skinner, who transformed the subject with “The Foundations of Modern Political Thought” (1978). Cambridge University Press in turn spied a niche academic market. To its splendid series of classic political texts, it is now adding a monumental, six-volume history. The first three, stretching from Greece and Rome to the 17th century, are already out. Now, leapfrogging the volumes for the 18th and 19th centuries, comes, chronologically, the final one, covering the 20th century.

The Cambridge History of Twentieth-Century Political Thought
Edited by Terence Ball and Richard Bellamy

Cambridge University Press; 766 pages; $140 and £95

Buy it at
Amazon.com
Amazon.co.uk

It is an impressive work of reference, accompanied by a 57-page bibliography and handy biographical sketches of 180 leading thinkers. The book's 27 essays fall into five parts: the changing fortunes of liberal democracy; the varieties of Marxism; a section called “Science, Modernism and Politics” (dealing among other things with post-modern continental thinkers and the Anglo-American school); new social movements (pacifism, identity politics, feminism and the Greens); and two essays on non-western thought, one general, the other focused on Islam. An epilogue explores the enduring left-right divide.

The first section coheres best, probably because the story's shape is clearest. In essence, it tells how 19th-century liberalism met the challenges of mass politics (and its perversions, fascism and communism) and why the answer, welfarism, itself came under challenge. The nearer to now, the less obvious the thread. This is not the editors' fault. Does anybody know?

Naturally, with 29 contributors, the standard varies. The level of exposition is generally high, though none of it is light reading. In the later sections, Melissa Lane on early responses to scientific positivism, Peter Dews on post-modernism and Bhikhu Parekh on non-western political thought, stand out. Editors of compilations face a trade-off between comprehensiveness and deadlines as contributors drop out—or drop dead. Commissioned over a decade ago, there was evidently pressure to push this volume out into a virgin market, even at the risk of leaving gaps.

Some are glaring. Conservatism gets 15 pages. Michael Oakeshott and Carl Schmitt, two (very different) opponents of liberalism, have eight brief mentions between them. Rational-choice theory, its derivatives and critics, rate barely a paragraph. In fact, the economic view of society (individualist variant), a new orthodoxy in political-science departments and law schools, is almost entirely neglected, while the economic view of society (Marxist variant) gets some 100 pages.

What is missing, however, should not detract from what is there. Even if bits are vague or blank, this is an indispensable map. If you care about politics and agree with Keynes that ideas matter, you will find this an essential reference tool.

The Cambridge History of Twentieth-Century Political Thought.
Edited by Terence Ball and Richard Bellamy.
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About sponsorship

Celibacy

When the vow breaks

Jan 15th 2004
From The Economist print edition

The consequences of the Roman Catholic church's policy

Get article background

CELIBACY is a very odd thing. Not only because it seems, at least from a secular, rational viewpoint, to mean giving up something that most people find natural and enjoyable; but also because the Roman Catholic church, which publicly insists on it for most of its clergy, underpins it with such shaky theological foundations.

There are telling exceptions: married men may become priests of the Uniate churches of eastern Europe, for example. The pope is head of their church too, and there are married quarters at the Vatican when they visit. Married Anglican clergy who feel abandoned by their church's rush to liberalism are also allowed to become Roman Catholic priests.

Richard Sipe is an authority on the subject and an influential critic of the church in America. His latest book is a timely and welcome look at the issue of celibacy, chiefly based on 1,500-plus anonymous interviews with priests and their sexual partners (in some cases victims). A former priest and a practising therapist, he outlines lucidly the theoretical and practical difficulties created by the church's policy.

Celibacy in Crisis: A Secret World Revisited
By A. W. Richard Sipe

Brunner-Routledge; 320 pages; $24.95

Buy it at
Amazon.com
Amazon.co.uk

Those for whom curiosity is the natural reaction to celibacy will find some of the stories in the book gratifying. There are some dreadful stories to be told, and Mr Sipe tells them. He is rightly cross with the way the church has handled the scandals that arise from broken vows of celibacy: pregnant nuns, ill-treated housekeeper-concubines, altar boys used as catamites. The Archdiocese of Birmingham in England this week agreed to pay £333,000 ($614,800) to a former altar boy who was sexually abused by a priest.

Coping with human failings is hard enough in a church that allows priests to marry. When they are not supposed to have sex of any kind, with anyone, anywhere, ever, then any approach to sexual ethics will be clouded by shame and secrecy from the start. The results have been horrid: not only does the rule of celibacy look inhuman and impractical, but the church has also suffered deeper damage: an organisation that preaches love and justice has been seen to practise neither.

But for all that, Mr Sipe is sympathetic to the idea of celibacy as a way to holiness—for those who feel comfortable with it. People who want to devote themselves wholly to the service of others may find that sex gets in the way. The real problem for the church, he argues, is not maintaining a mandatory policy that is widely and painfully ignored, but finding a new approach to sexuality that recognises both human weakness and divine purpose.

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By A. W. Richard Sipe.
Brunner-Routledge; 320 pages; $24.95

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The media industry

A question of values

Jan 15th 2004
From The Economist print edition

IN KEN AULETTA'S book about journalism, senior print journalists in America come across as pompous self-obsessives who lack a sense of humour. Even so, it is a rather fonder look at the profession than would be found, say, in the “Street of Shame” and “Hackwatch” pages of *Private Eye*, a satirical British magazine.

Backstory: Inside the Business of News
By Ken Auletta

The Penguin Press; 320 pages; $24.95

Buy it at
Amazon.com
Amazon.co.uk

“Backstory” is made up of 11 essays, ten of which were published in the *New Yorker* between 1993 and 2003, and one, on warring New York tabloids, which was rejected due to a “miscommunication” with editors. The theme that runs through many of them is the conflict between the business of journalism—selling advertisements and cutting costs—and editorial integrity and excellence. One essay wickedly asks prominent journalists to justify their sizeable earnings from public speaking.

Mr Auletta clearly has remarkable access to people at the top of his industry. But the price, too often, is that he gives them too much space to utter lofty thoughts that do not tell the reader much. He gives too little of his own analysis—especially about the business side of journalism. In an over-long interview with Howell Raines, a former editor of the *New York Times*, Mr Auletta allows Mr Raines to blow his own trumpet for more than 50 pages. He gives comparatively brief mention of Mr Raines's humiliating fall after Jayson Blair, a reporter, was found making up bits of his stories.

That said, at its best Mr Auletta's style is subtle and engaging, with fine use of detail. The book gets better as it goes along, and readers in a hurry could skip straight to the excellent final article on Fox News, which was published in 2003. Fox News's boss, Roger Ailes, says he dislikes journalists with a “pick up their ass” approach, who treat journalism as a “from-the-Mount profession”—a pertinent comment on the worthy characters who inhabit some of the other essays.

The public's trust in journalists is low. The American media in particular are under attack from some people for having a liberal bias, and from others for its blind patriotism during the war on Iraq. It is, therefore, disappointing that Mr Auletta, who has been described by the *Columbia Journalism Review* as America's foremost media critic, seems to prefer recycling old material rather than putting his energies into more original work.

Backstory: Inside the Business of News.
By Ken Auletta.
The Penguin Press; 320 pages; $24.95

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About sponsorship

Psychiatry

Prozac and Freud

Jan 15th 2004
From The Economist print edition

The clash between drugs and psychoanalysis

THE couch, that item of furniture that Sigmund Freud turned into a medical tool, fell into disuse with the development of drugs claimed to deal with psychotic problems. A new generation of psychiatrists dismissed psychoanalysis as being as dated as Marxism. Better to get a patient to pop a pill instead of listening to months, perhaps years, of chat about the patient's life. Psychiatry underwent a shift “from blaming the mother to blaming the brain”, said one observer. “Doctor please/Some more of these”, sang the Rolling Stones.

Of the succession of wonder drugs that came on the market, claiming to alleviate depression and associated illnesses, perhaps the most famous was Prozac. “America became a Prozac nation,” Jonathan Metzl writes. Forget about gender, sex, penises, all that psychoanalysis stuff. A person's temperament, it was claimed, was determined by genes and the chemicals in the brain. A drug could correct an imbalance.

Mr Metzl, a psychiatrist, has clearly been unhappy about all the scorn directed at the couch, typically in Todd Dufresne's book, “Killing Freud”. In this, the latest in a series of anti-Freud publications by Mr Dufresne, an academic, he dismisses support for psychoanalysis as “sentimental and superstitious”. His book is sometimes cruelly witty, but he has chosen an easy target, the psychiatrist or “trick-cyclist” of popular culture.

Mr Metzl seeks to strike a balance between the value of psychoanalysis and treatment by drugs. His book is a plea for a truce between those who deal with the mind and those who study the brain. In offering an engrossing history of psychiatry over the past 50 years, he seeks to show that there are indeed connections between Freud and Prozac. He applauds those psychiatrists who, while using biology, observe the importance of relationships between doctors and patients.

Mr Metzl would probably hate “The Mummy at the Dining Room Table”, if only for its come-on title. Yet the book is an interesting account of the survival of the couch into the Prozac era. The authors asked a number of psychiatrists to describe their most memorable cases; and some that had stuck in their memory tended to be of Freudian duration. One patient liked to tell stories of her eccentric family. She said that after a much-loved aunt died her body was embalmed so that she could remain with her grieving husband and their children, corporeally at least. The aunt had her own chair at mealtimes or while watching television. At the end of the day her husband would take her to bed. The psychiatrist said he greatly missed the stories when his patient's treatment ended.

Prozac on the Couch: Prescribing Gender in the Era of Wonder Drugs.
By Jonathan Michael Metzl.
Duke University Press; 275 pages; $24.95

Prozac on the Couch: Prescribing Gender in the Era of Wonder Drugs
By Jonathan Michael Metzl

Duke University Press; 275 pages; $24.95

Buy it at
Amazon.com
Amazon.co.uk

Killing Freud: Twentieth-Century Culture and the Death of Psychoanalysis
By Todd Dufresne

Continuum; 211 pages; $24.95 and £16.99

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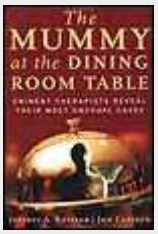
The Mummy at the Dining Room Table: Eminent Therapists Reveal Their Most Unusual Cases
By Jeffrey A. Kottler and Jon Carlson



Jossey-Bass; 325 pages; $24.95 and £14.99

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About sponsorship

A director's debut

It's my house

Jan 15th 2004
From The Economist print edition

A film of changing sympathies

VADIM PERELMAN'S “House of Sand and Fog” is about a homeless woman and an exiled Iranian air-force officer struggling for possession of a dilapidated California beach house. If the story sounds unappealing, remember that Steven Spielberg said he co-founded DreamWorks SKG so that he could give the green light to films like this. He can be proud that he did.

The film, which Mr Perelman scripted with Shawn Lawrence Otto from a novel by Andre Dubus, is his first feature-length work. It opens with Kathy (Jennifer Connelly), a recovering alcoholic, being evicted by the local authority from her house for non-payment of property tax. The house is bought for next to nothing by the Iranian (Ben Kingsley), who plans to sell it at a profit to pay for the college education of his son, Esmail (Jonathan Ahdout). To complicate matters, the policeman (Ron Eldard) who evicted Kathy has fallen for her and wants to play white knight.

Mr Perelman forces the viewer continually to change sides over the characters: first to side with Kathy and her handsome hero; then to shift sympathies and keep shifting. Unfolding like a thriller, the film keeps the viewer guessing about each new twist on the road to catastrophe. The final scene is one no viewer is likely to forget.

Mr Kingsley inhabits the Iranian's skin to perfection, while Ms Connelly more than holds her own in a difficult role. But the drama is anchored by the performance of Shohreh Aghdashloo as Mr Kingsley's wife. Responding gently each time Kathy lands on her doorstep like a wounded quail, Ms Aghdashloo paints a complex portrait of a Muslim woman that is the closest thing to a political statement to be found in this moving film.

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Italian painting

A touch of heaven

Jan 15th 2004
From The Economist print edition

THE Florentines, as one scholar has noted, took out a patent on the history of art. Ever since the 16th century, when Giorgio Vasari wrote “The Lives of the Artists” as a history that culminated with Florentine painting, art has been judged partly on his terms. This perhaps explains why Siena, Florence's rival in many ways, has been treated as an also-ran of art history. Now two fascinating new books on Sienese painting, as well as a recent exhibition, tell the story of early Italian art from the Sienese viewpoint, full of colour, emotion and narrative detail.

Its first great painter, Duccio di Buoninsegna (c.1255-1319), would have witnessed the emergence of the Nine: a civic democracy in which Siena, a rich merchant city-state, was ruled by nine elected citizens (aristocrats and lawyers were barred from standing for election). The Nine embarked upon a programme of urban renewal, adorning their new cathedral, building the city's civic palace, the vast piazza that spreads like a scallop shell before it, and the palatial hospital that still functioned in recent times.

Duccio trained alongside his Florentine contemporary, Giotto, in the workshop of Cimabue, the most famous Italian painter of his time. While Giotto developed a sense of volume in his painting, Duccio stuck to the two-dimensional painting of Cimabue and surpassed it, leavening the Byzantine forms with brilliant hues and a tenderness between Madonna and Child (pictured) that could touch his viewers.

Giotto and Duccio have been called the Picasso and Matisse of their day: Giotto the more epic, Duccio the more lyrical. Duccio's images are intended to move the heart not the mind. In the upper regions of his paintings, the glowing gold grounds create a heaven inhabited by the Madonna, while in the more earthly parts he depicts Siena as the new Jerusalem.

Duccio's art is always on display in his home town, where his masterpiece, the “Maestà” altarpiece, has pride of place in the cathedral museum and many of his key works hang in the Palazzo Pubblico and the Pinacoteca Nazionale. An exhibition in Siena that ended this week brought together works by Duccio and his followers that have been scattered around the world and also presented two recent Sienese discoveries about the art of Duccio's time: the cathedral's stained glass window, which restoration proves was both designed and painted by Duccio; and the unearthing in the cathedral of a 13th-century crypt, containing frescoes that are remarkably intact. No one yet knows whether Duccio had a hand in the frescoes, but they are yielding important clues about the colours and painting techniques of that era.

Sienese painting still speaks to us today because of its connection with the architecture and the history of the city in which it was born. For one luminous moment, Siena experimented with a utopian state and created an art to express it. In politics, its democracy survived for little more than 70 years. In paint, Siena has done rather better.

Sienese Painting: The Art of a City-Republic (1278-1477)
By Tim Hyman

Thames & Hudson; 224 pages; $16.95 and £8.95

Buy it at
Amazon.com
Amazon.co.uk

Painting in Late Medieval and Renaissance Siena (1260-1555)
By Diana Norman

Yale University Press; 320 pages; $40 and £25

Buy it at
Amazon.com
Amazon.co.uk

Sienese Painting: The Art of a City-Republic (1278-1477).
By Tim Hyman.
Thames & Hudson; 224 pages; $16.95 and £8.95

Painting in Late Medieval and Renaissance Siena (1260-1555).
By Diana Norman.
Yale University Press; 320 pages; $40 and £25

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About sponsorship

New fiction

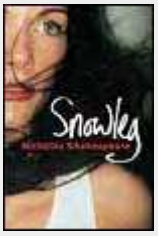
Betrayal in Berlin

Jan 15th 2004
From The Economist print edition

IT IS astonishing, given Germany's two centuries of war, its recent ideological fission and its subsequent struggle to become whole again, that many British novelists, John le Carré aside, have shown so little interest in setting their fiction there. All the more astonishing, as Nicholas Shakespeare's superb new novel illustrates so well, because the tensions between the two societies divided by the wall make for such a rich literary backdrop.

At the age of 16, Peter Hithersay discovers that far from being the honourable English schoolboy he has always assumed himself to be, he is half-German—and illegitimate. Curiosity about the unnamed East German that his mother briefly loved and lost draws Peter to read medicine at a West German university—probably the closest a westerner could get to studying in the East in 1986—which is where he encounters an amateur mime troupe. Accompanying the actors on a weekend visit to Berlin, Peter crosses the wall into the eastern sector and the course of his life is changed for ever.

Snowleg
By Nicholas Shakespeare



Harvill; 387 pages; £16.99

Buy it at
Amazon.com
Amazon.co.uk

Peter's number-one boyhood hero is Sir Bevidere, last knight of the Round Table whom the dying King Arthur entrusted with his sword, and he longs to meet a dragon-threatened damsel to whom he might display the courage he hopes he harbours within. In East Berlin, Peter meets a girl named Snowleg, and, in a heady moment, he promises to smuggle her to the West after the official dinner on the troupe's last night in the city. However, a single encounter with East German officialdom, in which, Judas-like, he denies having invited Snowleg to the feast, proves to Peter that he is not made of Arthurian stuff.

Snowleg vanishes, and Peter's road to perdition lies at the heart of Mr Shakespeare's new novel. But what makes this book so much more than just another thriller of betrayal and atonement is the sureness with which the author shapes and enriches his characters—you need supreme confidence to turn a paediatrician into a gerontologist halfway through a book. The all too East German subplot is never two-dimensional, but a rounded portrait of a society gone off-track in which men and women were bad, good and always human.

Mr Shakespeare's writing has grown with each new novel. “The Dancer Upstairs”, set in the Peru of the Shining Path terrorist group, proved conclusively that he was more than just a pen man for the Foreign Office, more than just another conjuror of the Englishman abroad. “Snowleg” is his finest book yet. Beautifully written, rich in character, it displays all the courage for which its hero so desperately wants to be recognised.

Snowleg.
By Nicholas Shakespeare.
Harvill; 387 pages; £16.99

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About sponsorship

Michael Straight

Jan 15th 2004
From The Economist print edition

Michael Straight, a reluctant whistle-blower, died on January 4th, aged 87

Ian Bradshaw

Get article background

TO THE end of his life, Michael Straight found it hard to admit that he had ever been a spy. Yes, as an employee in the State Department in 1938, he had passed reports to the Russians. But these had been his own analyses, containing nothing classified. Yes, he had sat in a parked car with Anthony Blunt, the "fourth man" of the Cambridge spy ring, while Blunt had torn a drawing in half and had informed him that the other half would be returned to him by his contact with the Kremlin. But Mr Straight thought this a bit of far-fetched drama. His eventual handler, "Michael Green" seemed to him a jolly man, courteous and fond of his food. It seemed undeserved that he was probably killed on Stalin's orders.

Mr Straight was both reluctant to be in this world, and strongly drawn towards it. Like so many others, he fell under the spell of communism in the 1930s, his enthusiasm moral and aesthetic as much as political. When he at last faced up to his past, in a book called "After Long Silence" (1983), he explained his student feelings in the words of John Maynard Keynes, who taught him economics at Cambridge:

> We were the forerunners of a new dispensation; we were not afraid of anything...nothing mattered except states of mind... timeless, passionate states of contemplation...one's prime objects in life were love, the creation and enjoyment of aesthetic experience and the pursuit of knowledge. Of these, love came a long way first...
>
> We were among the last of the Utopians...we repudiated all versions of original sin...

To this heady mix, Mr Straight added a potent sense of guilt about his background. He had been born into wealth and privilege in America, the son of an investment banker with an estate at Old Westbury, on Long Island. His parents, friends of the Roosevelts, believed in progressive thinking and social mixing; so each day the family chauffeur would deposit little Michael, his knees warmed by a Persian rug, at the door of a school in Harlem.

An English education followed. At the London School of Economics, where he went in 1933, he began to take an interest in the throngs of jobless northerners who were marching through the streets. But he could not stay late at political meetings, he told a friend, because he did not want to keep his brother's footman waiting.

Moving to Cambridge, Mr Straight was recruited first into the Cambridge Socialist Society and then into the Communist Party. He was not, he always said, a very ardent member. He sold copies of the *Daily Worker* round the university, but never had the "little green book" that would have marked him as a dedicated follower. Instead, his contacts grew through his membership of The Apostles, a tiny club that seemed dedicated mostly to drinking and good conversation. There he met Blunt, pale, elegant and art-loving, and the outrageously homosexual Guy Burgess, back in Cambridge to recruit Soviet agents. Mr Straight, however, insisted he never quite knew what Burgess was up to. The cherubic face did not seem to match "the black-rimmed fingernails...the dark, uneven teeth; the slouch; the open fly." Half-dazzled, half-repelled, Mr Straight tried to stay in the background.

But Blunt approached him. He was looking, he explained, for an American who might report back on "Wall Street's plans to dominate the world economy". Mr Straight did not take him too seriously, but did

not refuse. Back in America after 1937, he not only passed reports to “Michael Green” but helped another agent, Mark Geyn, to get press credentials as a journalist on the *New Republic*, the liberal magazine his parents had founded.

By 1941, Mr Straight had become the *New Republic*'s editor. His communist flirtations were far in the past, as far as anyone knew. In the 1948 election, the magazine supported Truman for president rather than Henry Wallace's lefter-leaning Progressive Party. During the McCarthy hearings in the 1950s, Mr Straight could write that “The Communist Party is a recruiting ground for subversion and espionage. Whoever joins it, either through guilty conscience or idealism, ends by losing all conscience and all ideals.” He was speaking of himself, though no one knew.

And his sense of guilt persisted. In 1963, when President Kennedy asked him to become his official adviser on art, memories of Blunt resurfaced. This “fourth man” had not been exposed, though Burgess had long since fled to Moscow; indeed, Blunt was now the Keeper of the Queen's Pictures. Mr Straight told the tale to the FBI, and then confronted Blunt himself. “We always wondered”, said his friend, “how long it would be before you turned us in.”

Yet Mr Straight had still not faced the truth about himself. Not until 1981, when he was telephoned by a reporter from Britain's *Sunday Times*, did he admit that he, too, had passed information to Russia. He could have exposed not only Blunt, but also Burgess, long before. A combination of loyalty, love and wilful blindness seems to have stopped him; that, and the knowledge that the trail also led to himself.

He could have told the truth in 1963, when he shopped Blunt. He was perhaps inhibited by the fact that the FBI man who took down his information, nodding sympathetically, was the son of his father's head gardener at Old Westbury.

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Overview

Jan 15th 2004
From The Economist print edition

America's unemployment rate fell to 5.7% in December from 5.9% in November. But the American economy was reckoned to have created only 1,000 new jobs in December, rather than the 150,000 that forecasters expected. Job growth in the current economic recovery has been slower than in most previous upturns.

America's **merchandise trade deficit** shrank sharply and unexpectedly in November to $44 billion, its lowest level in 13 months. American exports grew by 2.9% in November, while imports fell by 0.8%, thanks partly to a weaker dollar.

Canada's trade surplus fell in November, also thanks partly to a weaker greenback. Unemployment fell to 7.4% in December from 7.5% in November.

In the year to November, industrial output rose by 1.1% in **France**, by 1.0% in **Germany** and by 2.0% in **Spain**. Industrial production in **Austria** rose by 2.6% in the year to July. Wholesale prices fell by 0.1% in **Germany** in November.

Retail sales in **Japan** fell by 3.0% in the year to November.

Britain's unemployment rate fell in the three months to November to 4.9%, its lowest level in more than two years, thanks mostly to public-sector job growth. Industrial production fell by 0.5% in the year to November.

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Output, demand and jobs

Jan 15th 2004
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2003	2004	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 2.6	Q3	+ 4.8	+ 2.8	+ 3.6	+ 1.3	Q2	+ 5.3	Q3	5.6	Dec	6.1
Austria	+ 0.7	Q2	+ 1.1	+ 0.8	+ 1.9	+ 2.6	Jul	– 4.0	Aug	4.5	Nov	4.3
Belgium	+ 0.8	Q3	+ 2.2	+ 1.0	+ 1.9	– 4.8	Oct	+ 3.4	Oct	12.7	Dec†	11.7
Britain	+ 2.0	Q3	+ 3.1	+ 2.0	+ 2.8	– 0.5	Nov	+ 3.7	Nov	4.9	Nov††	5.2
Canada	+ 1.0	Q3	+ 1.1	+ 1.7	+ 3.1	– 0.3	Oct	+ 3.1	Sep	7.4	Dec	7.5
Denmark	– 0.5	Q3	– 0.8	+ 0.5	+ 2.2	– 1.5	Oct	+ 5.5	Oct	6.5	Nov	5.4
France	– 0.3	Q3	+ 1.5	+ 0.2	+ 1.9	+ 1.1	Nov	– 2.2	May	9.6	Nov	9.2
Germany	– 0.2	Q3	+ 0.9	– 0.1	+ 1.7	+ 1.0	Nov	– 2.5	Nov‡	10.4	Dec§	10.1
Italy	+ 0.5	Q3	+ 2.0	+ 0.5	+ 1.7	+ 0.4	Oct	– 0.4	Sep	8.4	Oct	8.9
Japan	+ 1.8	Q3	+ 1.4	+ 2.4	+ 2.1	+ 2.4	Nov	– 3.0	Nov	5.2	Nov	5.3
Netherlands	– 1.1	Q3	+ 0.5	– 0.7	+ 1.1	– 0.1	Oct	na	nil	5.7	Nov**	4.3
Spain	+ 2.4	Q3	+ 2.9	+ 2.4	+ 3.0	+ 2.0	Nov	+ 2.5	Sep	11.3	Nov	11.5
Sweden	+ 2.0	Q3	+ 1.9	+ 1.6	+ 2.5	+ 2.1	Oct	+ 3.9	Nov	3.9	Nov†	3.9
Switzerland	– 0.6	Q3	+ 1.0	– 0.4	+ 1.6	+ 0.4	Q3	– 4.0	Nov	4.1	Dec†	3.3
United States	+ 3.6	Q3	+ 8.2	+ 3.1	+ 4.5	+ 1.6	Nov	+ 8.3	Nov	5.7	Dec	6.0
Euro area	+ 0.3	Q3	+ 1.5	+ 0.5	+ 1.9	+ 0.9	Oct	nil	Oct	8.8	Nov	8.5
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 1.6	Q3	+ 3.2	na	na	+ 0.3	Nov	+ 3.6	Sep	8.2	Nov†	8.2
Greece	+ 5.0	Q3	+ 1.8	na	na	– 0.3	Aug	na		na		na
Iceland	+ 3.2	Q3	na	na	na	– 0.3	2002	na		2.8	Oct†	2.5
Ireland	+ 2.1	Q2	na	na	na	+11.5	Oct	+ 1.0	Oct	4.7	Dec	4.3
Luxembourg	+ 1.1	2002	na	na	na	+ 4.3	Oct	+ 2.0	Aug	4.1	Nov	3.3
New Zealand	+ 3.5	Q3	+ 6.3	na	na	+ 4.1	Q3	+ 6.1	Q3	4.4	Q3	5.4
Norway	+ 0.2	Q3	+ 3.3	na	na	+ 2.1	Nov	+ 1.6	Nov	4.7	Q3	3.8
Portugal	– 0.9	Q3	– 2.1	na	na	+ 1.4	Nov	– 0.7	Oct	6.3	Q3†	5.1

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡New series. ††Sep-Nov; claimant count rate 3.0% in Dec. §EU harmonised rate 9.2% in Dec. **Sep-Nov.

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Prices and wages

Jan 15th 2004
From The Economist print edition

% change on year ago

	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2003	2004	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 2.6	Q3	+ 3.2	+ 2.7	+ 2.3	– 0.1	Q3	– 0.2	+ 5.1	Q3	+ 3.6
Austria	+ 1.3	Nov	+ 1.7	+ 1.3	+ 1.2	+ 2.5	Dec	+ 0.8	+ 2.3	Nov	+ 2.2
Belgium	+ 1.7	Dec	+ 1.4	+ 1.5	+ 1.4	– 0.4	Nov	+ 1.4	+ 1.9	Q3	+ 2.1
Britain	+ 1.3	Nov*	+ 1.6	+ 2.8†	+ 2.5†	+ 1.8	Dec	+ 1.0	+ 3.5	Nov	+ 3.8
Canada	+ 1.6	Nov	+ 4.3	+ 2.7	+ 1.6	– 4.0	Nov	+ 2.3	+ 3.1	Sep	+ 2.4
Denmark	+ 1.4	Dec	+ 2.5	+ 2.1	+ 1.6	+ 0.6	Nov	+ 0.8	+ 3.6	Q3	+ 3.9
France	+ 2.2	Dec	+ 2.3	+ 2.1	+ 1.7	+ 0.7	Nov	+ 0.9	+ 3.0	Q3	+ 3.5
Germany	+ 1.1	Dec	+ 1.2	+ 1.1	+ 1.1	+ 1.3	Dec	+ 1.1	+ 2.1	Oct	+ 2.6
Italy	+ 2.5	Dec	+ 2.8	+ 2.8	+ 2.3	+ 1.1	Nov	+ 1.6	+ 2.5	Nov	+ 2.2
Japan	– 0.5	Nov	– 0.4	– 0.2	– 0.2	– 0.1	Dec	– 1.3	+ 0.6	Nov	+ 0.6
Netherlands	+ 1.7	Dec	+ 2.8	+ 2.2	+ 1.7	+ 2.6	Nov	+ 2.2	+ 1.4	Jan	+ 3.5
Spain	+ 2.6	Dec	+ 4.0	+ 2.9	+ 2.6	+ 1.3	Nov	+ 1.6	+ 3.1	Q3	+ 3.8
Sweden	+ 1.4	Nov	+ 2.3	+ 2.1	+ 1.5	– 1.6	Nov	– 0.8	+ 3.1	Oct	+ 3.1
Switzerland	+ 0.6	Dec	+ 0.9	+ 0.6	+ 0.5	– 0.2	Nov	– 0.4	+ 1.8	2002	+ 2.5
United States	+ 1.8	Nov	+ 2.2	+ 2.3	+ 1.5	+ 4.0	Dec	+ 1.2	+ 2.0	Dec	+ 3.2
Euro area	+ 2.1	Dec	+ 2.3	+ 2.0	+ 1.7	+ 1.4	Nov	+ 1.1	+ 2.9	Q2	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.5	Nov	+ 1.7	na	na	– 0.2	Nov	+ 1.1	+ 3.9	Q3	+ 4.1
Greece	+ 3.1	Dec	+ 3.4	na	na	+ 1.5	Sep	+ 1.9	na		na
Iceland	+ 2.4	Jan	+ 1.4	na	na	+ 3.5	Dec	+ 5.9	+ 5.5	Nov	+ 5.7
Ireland	+ 2.2	Nov	+ 4.8	na	na	– 8.4	Nov	– 3.0	+ 4.7	Q3	+ 6.0
Luxembourg	+ 2.1	Dec	+ 2.2	na	na	+ 0.7	Oct	+ 0.3	+ 5.0	Oct	– 0.1
New Zealand	+ 1.5	Q3	+ 2.6	na	na	+ 0.1	Q3	– 2.1	+ 2.3	Q3	+ 2.3
Norway	+ 0.6	Dec	+ 2.8	na	na	+ 0.7	Dec	+10.1	+ 4.3	Q3	+ 5.0
Portugal	+ 2.5	Nov	+ 4.0	na	na	– 0.3	Nov	+ 1.7	– 1.3	Oct	+ 0.6

* New series. RPI inflation rate in November: 2.5%. † RPI

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Portfolio poll

Jan 15th 2004
From The Economist print edition

Portfolio poll

4th quarter 2003

	Holdings by instrument, %			Equity holdings by area, %						
	Equities	Bonds	Cash	United States	Other Americas	Britain	Euro area	Other Europe	Japan	Other Asia
Credit Suisse PB	35	35 ▲	30† ▼	54 ▲	0	0	17	3	15	11 ▼
Henderson	65	30 ▼	5 ▲	52	3	6 ▼	18	3	15 ▲	3
ISIS	60	35 ▼	5 ▲	47 ▼	4	6	20 ▲	4	11 ▲	8
Julius Baer PB	45	42	13‡	46	5	8	15	7 ▲	11	8 ▼
Lehman Brothers	70	30	0	46 ▲	0	7 ▼	20	7 ▲	12 ▼	8 ▲
Robeco Group	50	50	0	53 ▼	3 ▼	11	15 ▲	5 ▼	10 ▲	3 ▲
Standard Life	55	45	0	56 ▼	3 ▼	12 ▼	13 ▲	3 ▲	9 ▼	4 ▲
Average	54	38 ▼	8 ▲	51 ▼	2 ▼	7 ▼	17 ▲	5 ▲	12 ▼	7 ▲
Neutral*				55 ▼	3 ▼	11 ▼	14	5 ▲	9 ▼	3 ▲

	Bond holdings by currency, %				
	Dollar	Yen	Sterling	Euro area	Others
Credit Suisse PB	89 ▲	0	0	11 ▼	0
Henderson	15 ▼	30 ▲	5	50 ▲	0 ▼
ISIS	40	0	8	41	11
Julius Baer PB	88	0	0	7	5
Lehman Brothers	41 ▼	18 ▼	4 ▲	33 ▲	4 ▼
Robeco Group	40 ▲	20 ▼	7 ▼	32 ▼	1 ▼
Standard Life	21 ▼	29	5 ▲	42 ▲	3 ▼
Average	48 ▲	14 ▼	4 ▲	31 ▼	3 ▼
Neutral*	20 ▼	29 ▲	5 ▼	40 ▼	6 ▲

▼▲ A change of 5% points or more on previous quarter

▼▲ A change of less than 5% points on previous quarter

* Morgan Stanley Capital International (developed) world equity index; Citigroup world government-bond index

† Of which 20% invested in alternative investments

‡ Of which 9% invested in alternative investments

The money managers in our quarterly portfolio poll remain cautious. During the fourth quarter, they have all kept the proportion of their portfolios devoted to global equities unchanged, although ISIS reduced its stake in American equities by five percentage points. Robeco and Standard Life also cut their exposure to American stockmarkets. One reason may be the continued prospect of a weaker dollar, which reduces the returns on dollar-denominated assets. Only Credit Suisse and Robeco increased their dollar-denominated bond holdings, with Robeco cutting its allocation of yen-denominated bonds by more than five percentage points. Robeco reduced as well its holdings of bonds denominated in sterling, euros and other currencies.

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Money and interest rates

Jan 15th 2004
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Jan 14th 2004)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 8.7	+13.0	Nov	5.49	4.83	5.23	5.55	5.32	6.37
Britain	+ 8.2	+ 7.0	Nov	3.97	4.00	4.17	4.65	4.46	5.44
Canada	+ 5.2	+ 6.0	Nov	2.46	2.69	2.82	4.55	5.01	6.07
Denmark	+ 8.1	+ 9.9	Nov	2.30	3.14	2.60	4.27	4.43	5.36
Japan	+ 4.1	+ 1.5	Dec	0.02	0.03	0.09	1.30	0.87	1.48
Sweden	+ 2.9	+ 3.6	Nov	2.60	3.63	2.75	4.56	4.73	3.39
Switzerland	+24.4	+ 8.5	Nov	0.24	0.64	-1.61	5.44	2.36	2.46
United States	+ 6.6	+ 4.6	Nov	1.04	1.29	1.62	3.98	4.07	5.70
Euro area†	+10.7	+ 7.4	Nov	2.09	2.83	2.42	4.11	4.19	3.89

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.88%, Japan No. 256 1.30%. Central bank rates: US fed funds 1.00%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 3.75%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jan 15th 2004
From The Economist print edition

1995=100

	Jan 6th	Jan 13th*	% change on one month	% change on one year
Dollar index				
All items	91.0	92.2	+ 3.7	+21.5
Food	87.4	90.0	+ 2.1	+15.3
Industrials				
All	95.8	95.1	+ 5.8	+30.5
Nfa†	91.7	93.1	+ 5.6	+22.0
Metals	99.3	96.8	+ 5.9	+38.2
Sterling index				
All items	78.8	78.6	– 1.9	+ 5.7
Euro index				
All items	93.9	94.8	nil	+ 0.6
Yen index				
All items	102.9	104.2	+ 2.4	+ 9.3
Gold				
$ per oz	422.25	424.75	+ 4.2	+20.7
West Texas Intermediate				
$ per barrel	33.62	34.36	+ 4.4	+ 6.0

* Provisional. † Non-food agriculturals.

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Stockmarkets

Jan 15th 2004
From The Economist print edition

Market indices

	Jan 14th	2003-04 high	2003-04 low	% change on one week	% change on record high	% change on Dec 31st 2002 in local currency	% change on Dec 31st 2002 in $ terms
Australia (All Ordinaries)	3,314.7	3,325.4	2,673.3	+ 0.1	– 3.6	+11.4	+53.7
Austria (ATX)	1,672.7	1,672.7	1,120.2	+ 3.8	– 3.7	+45.4	+75.8
Belgium (Bel 20)	2,346.5	2,346.5	1,426.6	+ 2.2	–36.3	+15.9	+40.0
Britain (FTSE 100)	4,461.4	4,513.3	3,287.0	– 0.3	–35.6	+13.2	+29.3
Canada (Toronto Composite)	8,403.8	8,405.1	6,228.6	+ 0.2	–26.2	+27.0	+55.5
Denmark (KBX)	224.6	224.6	145.0	+ 2.1	–25.6	+35.1	+62.9
France (SBF 250)	2,455.1	2,455.1	1,630.1	+ 1.2	–44.1	+19.6	+44.5
(CAC 40)	3,612.6	3,612.6	2,403.0	+ 1.4	–47.8	+17.9	+42.5
Germany (DAX)	4,055.2	4,055.2	2,203.0	+ 1.3	–49.7	+40.2	+69.4
Italy (BCI)	1,279.8	1,286.7	959.4	+ 0.8	–41.4	+17.2	+41.7
Japan (Nikkei 225)	10,863.0	11,161.7	7,607.9	+ 1.0	–72.1	+26.6	+41.8
(Topix)	1,058.0	1,105.6	770.6	+ 0.6	–63.3	+25.5	+40.5
Netherlands (AEX)	347.2	347.2	218.4	+ 2.1	–50.5	+ 7.6	+30.0
Spain (Madrid SE)	833.0	833.0	576.8	+ 0.9	–27.3	+31.4	+58.8
Sweden (Affarsvarlden Gen)	195.6	195.6	127.8	+ 3.8	–51.1	+34.7	+62.2
Switzerland (Swiss Market)	5,624.3	5,624.3	3,675.4	+ 0.7	–33.1	+21.5	+36.5
United States (DJIA)	10,538.4	10,570.5	7,524.1	+ 0.1	–10.1	+26.3	+26.3
(S&P 500)	1,130.5	1,130.5	800.7	+ 0.4	–26.0	+28.5	+28.5
(NASDAQ Comp)	2,111.1	2,111.8	1,271.5	+ 1.6	–58.2	+58.1	+58.1
Europe (FTSE Eurotop 300)*	979.5	979.5	682.7	+ 1.2	–42.6	+14.3	+38.1
Euro area (FTSE Ebloc 100)*	853.3	853.3	565.7	+ 1.6	–45.0	+18.8	+43.6
World (MSCI)†	1,059.7	1,059.7	710.8	+ 0.7	–26.9	+33.8	+33.8
World bond market (Citigroup)‡	612.6	614.9	518.6	+ 0.7	– 0.4	+16.6	+16.6

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.
‡Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jan 15th 2004
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2003	2004	Exchange rate trade-weighted† 1990=100 Jan 14th	year ago	Currency units per $ Jan 14th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2003‡
Australia	− 14.9	Nov	− 27.2	Q3	− 5.9	− 5.2	89.7	75.3	1.29	1.71	2.37	1.63	1.21	0.8
Austria	− 0.8	Sep	+ 0.8	Oct	− 0.1	− 0.1	102.8§	101.1	0.79	0.94	1.45	–	0.74	-1.3
Belgium	+ 20.7	Oct	+ 9.9	Sep	+ 4.4	+ 4.4	102.9§	100.4	0.79	0.94	1.45	–	0.74	0.2
Britain	− 73.5	Nov	− 36.1	Q3	− 1.9	− 1.9	102.8	103.5	0.54	0.62	–	0.69	0.51	-2.9
Canada	+ 41.1	Nov	+ 16.7	Q3	+ 1.9	+ 1.5	88.9	76.6	1.29	1.54	2.37	1.64	1.22	1.0
Denmark	+ 10.2	Oct	+ 5.4	Oct	+ 2.9	+ 2.7	107.1	104.2	5.87	7.02	10.8	7.45	5.54	0.8
France	+ 4.6	Nov	+ 21.3	Oct	+ 1.3	+ 1.3	106.3§	103.4	0.79	0.94	1.45	–	0.74	-4.0
Germany	+142.6	Nov	+ 56.2	Nov	+ 2.4	+ 2.6	103.8§	100.4	0.79	0.94	1.45	–	0.74	-4.1
Italy	+ 3.4	Oct	− 19.2	Oct	− 1.1	− 1.0	75.8§	73.7	0.79	0.94	1.45	–	0.74	-2.7
Japan	+102.5	Nov	+132.0	Nov	+ 3.0	+ 3.0	136.7	133.3	105	118	155	134	–	-7.4
Netherlands	+ 33.0	Oct	+ 17.7	Q3	+ 2.9	+ 3.2	102.3§	99.5	0.79	0.94	1.45	–	0.74	-2.4
Spain	− 51.1	Oct	− 24.1	Sep	− 2.3	− 2.3	77.0§	75.3	0.79	0.94	1.45	–	0.74	0.1
Sweden	+ 17.9	Nov	+ 14.8	Q3	+ 4.6	+ 4.4	81.6	78.4	7.24	8.66	13.3	9.18	6.83	0.2
Switzerland	+ 6.2	Nov	+ 29.4	Q3	+10.8	+10.7	111.8	116.2	1.23	1.38	2.26	1.56	1.16	na
United States	−548.6	Nov	−541.7	Q3	− 5.0	− 5.3	93.8	109.2	–	–	1.84	1.27	0.94	-4.9
Euro area	+ 86.7	Oct	+ 42.1	Oct	+ 0.4	+ 0.6	92.4	85.1	0.79	0.94	1.45	–	0.74	-2.7
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 13.4	Nov	+ 10.9	Oct	na	na	81.6§	79.3	0.79	0.94	1.45	–	0.75	2.6
Greece	− 24.8	Oct	− 10.7	Oct	na	na	59.4§	58.2	0.79	0.94	1.45	–	0.75	-1.6
Iceland	− 0.2	Nov	− 0.4	Q3	na	na	92.9**	91.9	70.0	79.7	129	88.7	66.0	-1.0
Ireland	+ 38.6	Oct	− 2.1	Q3	na	na	94.5§	89.8	0.79	0.94	1.45	–	0.75	-1.0
Luxembourg	− 3.4	Oct	+ 2.0	Q3	na	na	102.9§	100.4	0.79	0.94	1.45	–	0.75	-0.3
New Zealand	− 1.8	Nov	− 3.3	Q3	na	na	105.3	94.7	1.49	1.86	2.73	1.89	1.40	2.6
Norway	+ 28.0	Nov	+ 28.4	Oct	na	na	95.0	108.0	6.78	6.90	12.5	8.60	6.40	9.8
Portugal	− 13.0	Oct	− 7.8	Sep	na	na	93.2**	91.1	0.79	0.94	1.45	–	0.75	-2.9

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, November average. ‡OECD estimate.

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Government bonds

Jan 15th 2004
From The Economist print edition

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Overview

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From The Economist print edition

Singapore's GDP grew at an annual rate of 7.9% in the fourth quarter; its 12-month rate of growth quickened to 3.7%.

Inflation in **Brazil** fell to 9.3% in the year to December, down from 17% in May. But industrial production continues to stagnate, rising by only 0.3% in the year to November. **Mexico's** economy is also struggling: output fell by 0.3% over the same period.

Israel's trade deficit narrowed to $6.0 billion in 2003, its smallest for 12 years.

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The Big Mac index

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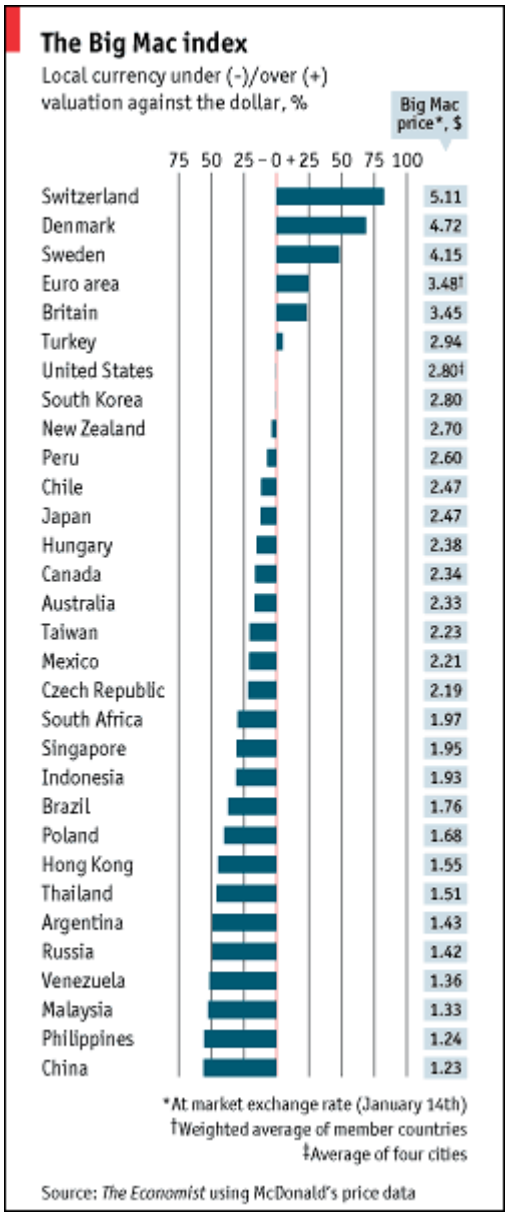
The Economist's Big Mac index is based on the theory of "purchasing-power parity". Under PPP, exchange rates should adjust to equalise the prices of a basket of goods and services across countries. Our basket is the Big Mac. For example, the cheapest burger is in China, at $1.23, compared with an average American price of $2.80. This implies the yuan is 56% undervalued. Relative to its Big Mac PPP the euro is 24% overvalued against the dollar. In contrast, the yen is 12% undervalued.



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Economy

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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.1	Q3	+17.9	Nov	+ 3.0	Nov	+22.9	Nov	+35.4	2002	406.0	Oct
Hong Kong	+ 4.0	Q3	– 9.2	Q3	– 2.3	Nov	– 8.0	Nov	+16.7	Q3	118.4	Dec
India	+ 8.4	Q3	+ 7.4	Nov	+ 3.1	Nov	–13.8	Nov	+ 2.3	Q3	96.6	Dec
Indonesia	+ 3.9	Q3	+ 4.7	Jul	+ 5.1	Dec	+26.8	Nov	+ 8.1	Q2	33.8	Nov
Malaysia	+ 3.5	Q3	+11.7	Nov	+ 1.2	Dec	+19.3	Nov	+11.9	Q3	44.0	Nov
Philippines	+ 4.4	Q3	– 3.9	Oct	+ 3.1	Dec	– 1.4	Oct	+ 3.4	Sep	13.4	Dec
Singapore	+ 3.7	Q4	+ 7.7	Nov	+ 0.6	Nov	+15.7	Nov	+25.6	Q3	96.3	Dec
South Korea	+ 2.3	Q3	– 3.9	Nov	+ 3.4	Dec	+14.4	Dec	+ 9.8	Nov	150.3	Nov
Taiwan	+ 4.2	Q3	+ 6.7	Nov	– 0.1	Dec	+17.0	Dec	+28.8	Q3	206.6	Dec
Thailand	+ 6.5	Q3	+ 7.4	Nov	+ 1.8	Dec	+ 4.5	Nov	+ 8.1	Nov	40.2	Nov
Argentina	+ 9.8	Q3	+13.0	Nov	+ 3.7	Dec	+16.6	Nov	+ 8.9	Q3	14.1	Dec
Brazil	– 1.5	Q3	+ 0.3	Nov	+ 9.3	Dec	+24.8	Dec	+ 3.7	Nov	54.4	Nov
Chile	+ 3.0	Q3	+ 1.5	Nov	+ 1.1	Dec	+ 2.9	Dec	– 0.3	Q3	15.9	Dec
Colombia	+ 4.0	Q3	+ 2.3	Oct	+ 6.5	Dec	– 0.2	Oct	– 1.6	Q3	10.5	Dec
Mexico	+ 0.4	Q3	– 0.3	Nov	+ 4.0	Dec	– 5.6	Nov	–10.5	Q3	57.3	Nov
Peru	+ 4.1	Oct	+ 0.7	Oct	+ 2.5	Dec	+ 0.5	Oct	– 1.2	Q3	9.6	Nov
Venezuela	– 7.1	Q3	– 4.8	Oct	+27.1	Dec	+14.0	Q3	+ 8.9	Q3	14.2	Sep
Egypt	+ 3.1	2003†	+ 4.2	2002†	+ 5.2	Oct	– 6.0	Jul	+ 3.3	Q3	13.3	Aug
Israel	+ 2.8	Q3	– 4.9	Oct	– 2.0	Nov	– 6.0	Dec	– 0.2	Q3	26.1	Dec
South Africa	+ 1.6	Q3	– 3.8	Nov	+ 0.4	Nov	+ 2.0	Nov	– 1.3	Q3	6.5	Nov
Turkey	+ 4.8	Q3	+ 3.9	Nov	+18.4	Dec	–20.9	Oct	– 5.6	Oct	31.3	Nov
Czech Republic	+ 3.4	Q3	+ 5.2	Oct	+ 1.0	Dec	– 2.4	Nov	– 7.8	Q3	27.0	Dec
Hungary	+ 2.9	Q3	+ 9.7	Nov	+ 5.6	Nov	– 4.3	Nov	– 5.5	Oct	12.8	Dec
Poland	+ 3.9	Q3	+ 9.1	Nov	+ 1.6	Nov	– 9.5	Nov	– 2.9	Nov	32.6	Dec
Russia	+ 5.7	Q3	+ 7.1	Nov	+12.0	Dec	+58.9	Nov	+39.1	Q4	73.2	Dec
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 4.6	Q3	+ 9.1	Oct	+ 1.1	Dec	– 1.9	Nov	– 1.5	Q3	1.1	Nov
Latvia	+ 7.3	Q3	+ 1.0	Nov	+ 3.6	Dec	– 2.0	Nov	– 0.9	Nov	1.4	Nov
Lithuania	+ 8.4	Q3	na		– 1.3	Dec	– 2.4	Nov	– 1.1	Q3	3.0	Nov
Slovakia	+ 4.2	Q3	+ 4.1	Nov	+ 9.2	Dec	– 0.6	Nov	– 0.8	Sep	10.9	Nov
Slovenia	+ 2.3	Q3	+ 2.4	Nov	+ 4.6	Dec	– 0.6	Sep	+ 0.1	Oct	8.0	Oct
Pakistan	+ 5.1	2003†	+ 9.9	Aug	+ 5.4	Dec	– 1.3	Dec	+ 3.6	Q3†	10.8	Nov
Saudi Arabia	+ 1.0	2002	na		– 1.2	Jul	+41.8	2002	+11.9	2002	24.5	Nov

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank.

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Financial markets

Jan 15th 2004
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jan 14th		Dec 31st 2002	
	Jan 14th	year ago	Jan 14th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	15.2	na	1,668.9	+0.3	+ 17.6	+ 17.6
Hong Kong	7.76	7.80	14.3	0.08	13,320.9	+1.2	+ 42.9	+ 43.5
India	45.4	47.9	83.4	4.24	6,194.1	+4.0	+ 83.4	+ 93.8
Indonesia	8,343	8,865	15,337	8.49	756.6	+6.7	+ 78.0	+ 91.0
Malaysia	3.80	3.80	6.99	3.03	816.0	+1.3	+ 26.3	+ 26.3
Philippines	55.5	53.5	102.0	7.63	1,525.3	+0.6	+ 49.8	+ 44.1
Singapore	1.70	1.73	3.12	0.75	1,860.5	+1.3	+ 38.7	+ 42.0
South Korea	1,180	1,173	2,170	4.27	849.6	+2.7	+ 35.4	+ 36.1
Taiwan	33.6	34.4	61.8	1.15	6,275.0	+2.2	+ 40.9	+ 45.7
Thailand	39.0	42.7	71.7	1.34	790.8	+5.3	+121.8	+145.1
Argentina	2.87	3.22	5.28	4.06	1,202.3	+3.4	+129.0	+168.3
Brazil	2.82	3.31	5.18	16.33	23,398.6	+0.3	+107.7	+160.7
Chile	574	719	1,055	2.28	7,275.7	+0.9	+ 44.9	+ 82.0
Colombia	2,745	2,911	5,046	7.96	2,425.6	−1.2	+ 50.8	+ 57.5
Mexico	10.8	10.5	19.9	4.92	9,171.7	+0.8	+ 49.7	+ 44.7
Peru	3.46	3.49	6.36	2.51	2,734.7	+9.7	+ 96.5	+ 99.7
Venezuela	2,934§	1,692	5,393	20.04	25,856.9	+9.4	+222.6	+ 52.5
Egypt	6.16	4.59	11.32	6.89	12,592.2	+3.0	+134.4	+ 76.2
Israel	4.42	4.83	8.13	1.61	565.8	+2.8	+ 70.2	+ 82.9
South Africa	7.11	8.80	13.1	7.95	10,943.4	+4.1	+ 18.0	+ 42.4
Turkey	1,354,000	1,672,500	2,489,058	23.00	18,818.5	−2.9	+ 81.5	+122.5
Czech Republic	25.7	30.1	47.2	2.07	676.9	+0.4	+ 46.9	+ 72.0
Hungary	210	221	385	12.52	9,571.3	−0.3	+ 22.7	+ 31.7
Poland	3.74	3.80	6.88	5.22	22,012.3	+0.2	+ 53.2	+ 57.0
Russia	28.9	31.8	53.1	16.00	595.2‡	+0.4	+ 49.9	+ 65.8
EMF (MSCI)*	1.00	1.00	1.84	na	464.1	+0.9	+ 58.9	+ 58.9
EMBI+†	1.00	1.00	1.84	na	302.3	+0.7	+ 32.1	+ 32.1

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡ In $ terms. § Floating exchange rate

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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